BLOCKBUSTERS

HIT-MAKING, RISK-TAKING, AND THE BIG BUSINESS OF ENTERTAINMENT

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Prologue

SHOW BUSINESS—A BUSINESS OF BLOCKBUSTERS

In 1999, Alan Horn, new in his role as president and chief operating officer of the film and television studio Warner Bros., embarked on a high-stakes strategy. Entrusted with the power to decide which movies the studio would make—the coveted "greenlighting" decision—he chose to single out four or five so-called tent-pole or event films—those thought to have the broadest appeal—among its annual output of around twenty-five movies, and support those picks with a disproportionately large chunk of its total production and marketing budget. Other studio heads had produced daring, big-budget movies before, of course, but no one had, as Horn put it, "really pursued it as a strategy"—none had, in other words, dared to make a handful of such big bets each year, at the expense of the attention lavished on a larger number of smaller movies. "In the movie business, the product is the same price to the consumer regardless of the cost of manufacturing it—whether its production budget is $15 million or $150 million. So it may be counterintuitive to spend more money," Horn told me. "But in the end, it is all about getting people to come to the theater. The idea was that movies with greater production value should be more appealing to prospective moviegoers. Audiences respond to movie stars, but those lead to higher costs. Audiences respond to special effects, but those lead to higher costs, too. And you have to let audiences know you are there with your movie—really market it as an event—but that of course further adds to the costs. You can only do so many of those big films in a given year."

Over the next few years, as Horn's strategy played out at Warner Bros., another executive was quickly moving up the ranks at a rival media conglomerate. Jeff Zucker, a former field and executive producer of *The Today Show*, climbed up to president and later chief executive officer of NBC's Television Group, overseeing what was then the number-one-rated television network in the United States. In 2007, after taking the reins at parent company NBC Universal, he led a push to cut the rising costs of programming at the television network—in many ways the exact opposite of Horn's strategy at Warner. "We're managing for margins instead of ratings," asserted Ben Silverman, whom Zucker had appointed as co-chair of NBC Entertainment. Fresh off a career as a high-flying television producer in his own right, Silverman was seemingly taking all the right measures to increase profits and reduce risk in his new role as a network executive: betting less on the most expensive dramatic content and instead focusing on intellectual property and formats that could be acquired at more reasonable prices; relying less on A-list actors and producers who could command fees of sometimes hundreds of thousands of dollars per episode; and cutting back on pilots that often came with a price tag several times that of a regular episode but generally did little to gauge true demand for a new series.

By 2011, Horn could look back on an unparalleled winning streak: under his leadership, Warner Bros. became the only studio in history to surpass $1 billion at the domestic box office for eleven years in a row. All indications are that profits had seen a strong upward trajectory as well, helped by smash hits such as the *Harry Potter* movies, *The Dark Knight, The Hangover* and its sequel, *Happy Feet, Million Dollar Baby, Ocean's 11* and its two sequels, and *Sherlock Holmes*. Alan Horn's stock had risen so high that when Walt Disney in 2012 was looking for a new executive to bring the magic

back to its troubled studio, it recruited Horn—only a year after his retirement from Warner Bros.—to take over as Walt Disney Studios' chairman. "He's earned the respect of the industry for driving tremendous, sustained creative and financial success," Disney's chief executive officer Bob Iger said.

And Zucker? His strategy failed miserably, and in 2010 he was asked to leave his high-profile job. But the damage had been done: NBC was farther behind on all the metrics that mattered—including, by all accounts, the profit margins Zucker and Silverman sought most. During Zucker's tenure, NBC fell from its perch as the highest-rated television network to fourth place, behind its three broadcast rivals—ABC, CBS, and FOX—a demise once unthinkable for the network that built its reputation on its "must-see" prime-time lineup. One rival executive labeled Zucker "a case study in the most destructive media executive ever to exist." While that may be too strong a statement, it is clear that his "managing for margins" strategy had disastrous results.

Warner's approach, which is the very strategy that NBC sought to escape, seems to fly in the face of conventional business rules. Why would film or television executives choose to put themselves in a position where their company's overall performance—or even survival—rests on a few big product launches each year, and let spending on those products reach levels that make recovering costs appear almost impossible? Especially in an industry in which audience demand is fickle and the failure rate is so high, would it not be more sensible in the long run to forgo these kinds of outsize investments and instead place a larger number of smaller bets, closely guard costs, and "manage for margins"?

Quite the contrary: what Warner Bros., NBC, and many other entertainment businesses have found out—often the hard way—is that a "blockbuster strategy" works. The leading television networks, film studios, book publishers, music labels, video game publishers, and producers in other sectors of the entertainment industry thrive on making huge investments to acquire, develop, and market concepts with strong hit potential, and they bank on the sales of those to make up for the middling performance of their other content. That is one of the essential lessons I have learned from studying these businesses: rather than spreading resources evenly across product lines (which might seem to be the most effective approach when no one knows for sure which products will catch on) and vigorously trying to save costs in an effort to increase profits, betting heavily on likely blockbusters and spending considerably less on the "also rans" is the surest way to lasting success in show business.

Blockbuster strategies are certainly not free of risk—even the biggest productions supported by the highest advertising budgets can, and sometimes will, fail to create a splash in the market. Just ask the people who thought investing in the 2012 movie *John Carter* was a great idea, or those who felt the television show *Lone Star* would make audiences tune in en masse that same year. In today's fragile economy, a world in which a high-profile business executive's every move is scrutinized by traditional news media and bloggers alike, appearing to play it safe may be a top priority. But content producers can't afford to walk away from big bets—doing so would actually *increase* their chance of failure in the long run. The highest-performing entertainment businesses take their chances on a small group of titles and turn those choices into successes by investing heavily in their development, supporting them with a high level of promotional spending, often well in advance of their release into the marketplace ("coming soon to a theater near you"), and distributing them as widely as possible. It may not look anything like the way products in other sectors of the economy are introduced, but it works.

In this book, I will do more than simply present evidence of the higher returns of blockbuster strategies. I will also try to explain *why* they are so effective and describe what is likely to go wrong when entertainment companies stop playing the blockbuster game and instead shift their focus to what may appear to be more risk-averse strategies, much like NBC did. As a professor at the Harvard Business School, I have studied media, sports, and other entertainment sectors for a decade. Over the years, I have heard all kinds of theories about why the entertainment industry is organized the way it is, or how it can be run better. And with the advent of digital technology that makes it possible for virtually everyone to become a content producer and share their creations with the world, there is much speculation about how the entertainment landscape might change, for the better or for the worse. "Old media" are dead in the water, some say. Studios will learn to stop betting on expensive projects and overpaid actors, instead taking "more shots at goal" with inexpensive ideas. Musicians will be freed from the shackles of record labels. Sports leagues will no longer need the likes of ESPN and will go directly to consumers via the Web. Once consumers are able to consume whatever they want, whenever they want it, they will migrate away from the hits. Or they will opt for the lowest-common-denominator content, ruining our culture. Paying for content is old-fashioned—free is the future. The list goes on and on.

My goal in this book is to separate fact from fiction—to describe how the entertainment industry really works, based on an understanding of why entertainment executives make the decisions they make and on actual data about how those decisions play out in the marketplace. In my role at the Harvard Business School, I am in the fortunate position to have been granted rare access to executives who make these kinds of decisions on a regular basis—sometimes while they are in the process of making them. I have worked on dozens of case studies of companies and people in film, television, music, publishing, sports, and other sectors of entertainment, and have conducted numerous one-on-one interviews and other conversations with practitioners (and spent an inordinate amount of time visiting film premieres, sports events, and other celebrity get-togethers—the kinds of sacrifices one has to make in the name of research). Drawing on my observations from the field, as well as on an expansive body of scholarly research, I will use these pages to try to get to the bottom of why media executives do what they do and how their strategies pan out. (If the word *scholarly* scared you in this last sentence, please don't worry—I promise to avoid all mentions of the fancy econometric and statistical techniques that were used to analyze sales patterns, and to concentrate squarely on the results that matter.)

As it turns out, how executives can best deal with risk is similar across the worlds of film, television, music, book publishing, sports, and other entertainment sectors. The lessons learned about blockbusters in film and television also apply to the rest of the entertainment industry. For instance, as I will show, many of the principles that underlie Warner Bros.' winning streak also explain why Grand Central Publishing could seriously consider making what some dismissed as an outrageously high bid for the rights to a manuscript about a fluffy creature, seemingly giving the publisher little more than an outside shot at recovering its investment. Or how Marvel Entertainment's Spider-Man, The Avengers, and other superheroes could turn into Hollywood executives' safest bets, leading to great riches for the company. And the same lessons capture how a certain Stefani Germanotta, also known as Lady Gaga, could catapult into the public's consciousness and, in just a couple of short years, become one of the planet's biggest celebrities. Or how a small New York–based record label could give rise to best-selling band Maroon 5, scoring one hit after another. Across these case studies, a consistent picture emerges of how businesses that want to maximize revenues and profits can best approach the production and marketing of entertainment products. And even though some cases go back a few years, the underlying issues are as true today as they were then. Anyone who works in show business should take note of these lessons—or, as NBC under Zucker did, ignore them at their peril.

Those who follow the world of entertainment as fans may find learning about these principles worthwhile, too, for they will determine what tomorrow's entertainment offerings will look like. Some of the lessons may be a bit disheartening to consumers who dislike the blockbuster mind-set of established entertainment companies and would rather see them invest in more niche offerings or unproven talent. But the purpose of this book is not to pass judgment on what makes for "good" or "bad" products, or to question purely creative decisions; there's no arguing about taste, after all.

Instead, the focus here is on explaining why entertainment markets work the way they do and what strategies will help build thriving, lasting businesses—the kinds of businesses, in other words, that deliver the types of products that vast numbers of people enjoy.

Zucker and Silverman are long gone at NBC, but the network is still recovering. It has dramatically changed its approach. After Zucker's departure, NBC Universal Television's new chairman, Jeff Gaspin, acknowledged that the "managing-for-margins" strategy had run its course and promised agents, producers, and other television industry insiders that the network would be back in the hunt for the next blockbuster hit. Now "in it to win it," as Gaspin put it, NBC's new goal was to put the best possible programs on the air. The network has been breaking the bank to do so. For the fall 2010 television season, it ordered an almost-unheard-of thirteen new series, including big-budget series from A-list producers like J. J. Abrams, Jerry Bruckheimer, and David E. Kelley. The network spent a rumored $150 million in development costs for that season alone and significantly increased its marketing costs in an effort to win back viewers. The next season, it further upped the ante. Taking cues from FOX and its blockbuster hit *American Idol*, NBC bet big on the talent show *The Voice*, paying more than $2 million per episode—and found a genuine hit of its own. In fact, helped by a favorable placement immediately after the 2012 Super Bowl, in February 2012 *The Voice* displaced *American Idol* as America's top-rated television series, causing NBC executives to crow about "an electricity in the building" at the company's headquarters at Rockefeller Center. One top rating for the network does not mean it has returned to its glory days, but it does appear that NBC's new executives have a better idea of what it might take to get there.

At Warner Bros., NBC, and many other entertainment companies, blockbuster strategies often go hand in hand with huge investments in top creative talent. Movie studios handsomely reward superstar actors such as Johnny Depp, Jennifer Lawrence, Will Smith, Kristen Stewart, and Robert Downey Jr. in hopes of converting fans of those stars into audiences for the studios' productions.

The same goes for television networks, with lead actors on the most successful series earning high six-figure salaries for each episode filmed. *The Voice*, for instance, was stacked with A-listers when it launched: the four judges—Christina Aguilera, CeeLo Green, Maroon 5's Adam Levine, and Blake Shelton—were all established stars in the world of music and could command sizable salaries.

The focus on star talent now extends into virtually all sectors of the entertainment industry. Openly admitting that he was taking a page from the book written by major Hollywood studios a year after Alan Horn started his event-film strategy, a Spanish businessman single-handedly raised the bar for investments in A-list talent in the world of soccer. Bringing a show-business mentality to his renowned soccer club, Real Madrid's president, Florentino Pérez, started pursuing what he called his *Galácticos* strategy, a reference to the star power of the players he sought to recruit. At the height of Galacticism, Englishman David Beckham, one of the sport's biggest icons, joined a team that was already brimming with stars from all over the globe. A marketer's dream, for sure, but also a very expensive dream. Are the high fees paid for star talent justified?

A close look at the market for creative talent and the ways in which studio heads, soccer-club presidents, and other entertainment managers decide on these matters reveals that there are good reasons to pay top dollar for star talent (and, admittedly, some not-so-good reasons). Betting on star talent creates important marketing advantages, drawing audiences and sponsors alike. But the competition for the few stars at the top is so severe that the pressure on entertainment businesses is getting pretty intense: the truth is that often they can barely afford to compete for the most sought-after performers, but at the same time they cannot afford *not* to do so. The tug-of-war between stars and entertainment companies, with each party vying for a bigger piece of the revenues and profits generated by blockbuster products, is one of the most fascinating aspects of today's entertainment economy—and one with great consequences for the future of show business.

As with any tug-of-war, offering accurate predictions about

who ultimately will be victorious requires a thorough understanding of each side's strengths and weaknesses as well as its strategies. Providing such insights is another major objective of this book, which is why I take a close look at the business models of star-focused enterprises like the major Hollywood studios and Real Madrid. I also give considerable attention to companies that take a different approach and instead specialize in developing promising talent into stars. Argentine soccer club Boca Juniors and Real Madrid's archrival FC Barcelona, for example, are both famous for fostering some of the world's best soccer players. And NBC's *Saturday Night Live*, one of television's longest-running shows, has served as a stepping-stone for dozens of A-list comedians, from Eddie Murphy and Adam Sandler to Jimmy Fallon and Tina Fey. One axiom becomes very clear: entertainment companies go to great lengths to gain the upper hand in their ongoing dealings with creative talent.

Such efforts don't come about in a vacuum, of course: superstars and the people who advise them are getting smarter about wielding their power. Recognizing their outsize value, talented actors, musicians, athletes, and other performers are pushing for ever-higher rewards. That, in turn, is putting pressure on the business models of studios, record labels, sports teams, and other content producers. Both sides have gotten ever more creative in their efforts to negotiate favorable agreements. And so it could come to be that, in 2006, even when his status as a star actor was first being challenged, the venerable studio MGM made a stunning move by offering Tom Cruise a part of a movie *studio* rather than a part in a movie—an ownership stake in MGM's United Artists, to be precise. Or that Russian tennis player Maria Sharapova forged lucrative endorsement partnerships with an impressive set of brands, leading her to become the highest-paid female athlete in the world (and beating out a stellar cast of male athletes, too). And that, to the astonishment of many sports-industry insiders (even before his much-debated decision to "take his talents to South Beach," as he described his move to the Miami Heat), basketball superstar LeBron James established his own firm to handle all aspects of his business ventures and marketing activities, taking a highly innovative approach to sports marketing.

My research shows that there is a clear logic to these developments, one that can be grasped by closely studying the characteristics of the market for creative talent as well as the talent's appetite for risk at different stages of their career. It is a logic that those who work in entertainment should be intimately aware of, as it yields lessons about how businesses can best recruit, manage, and reward talent—even if not every decision turns out as well as those involved might have hoped. It also offers important clues to any aspiring musician, actor, author, or athlete who wants to discover the best approach to his or her creative career. For superstars and lesser-known talent alike, knowing when to pursue which opportunities is critical, especially because the careers of most creative people are so short-lived.

All of this now transpires in a media environment that, with the arrival of the YouTube, Twitter, and Facebook era, is of course vastly different from what it was when Alan Horn and Jeff Zucker first dreamed up their strategies, and when Lady Gaga and LeBron James first emerged on the scene. Undoubtedly, the biggest question currently facing entertainment companies is how the rapid rise of digital technology will affect their bets on blockbusters and superstars. Because advances in digital technology substantially lower the cost of doing business, there are good reasons to suspect that far-reaching changes are on the horizon. New technologies, after all, make it easier and cheaper for content producers to offer entertainment goods—just think of the savings that result from distributing a movie online rather than having to transport physical prints to theaters all over the world. At the same time, new technologies, such as sophisticated recommendation engines, make it less of a hassle for consumers to find and purchase the goods they want. These effects are especially apparent in the entertainment sector, where goods like films, television shows, books, and music can be fully digitized.

Some industry insiders have suggested that digital technology will spell the end of blockbusters—and, with that, the effectiveness of blockbuster strategies. Is the rise of online distribution channels a sign that soon the "old" rules of the entertainment business will no longer apply? Looking at the popularity of sites such as YouTube that democratize content production and distribution, one might be tempted to conclude that a "yes" is the only right answer. But a closer look reveals that the reality isn't quite so simple. In fact, in today's markets where, thanks to the Internet, buyers have easy access to millions and millions of titles, the principles of the blockbuster strategy may be more applicable than ever before. As I will describe in the latter half of this book, there are fundamental laws of consumer behavior that explain the strategy's enduring appeal—the kinds of laws everyone with an interest in the entertainment industry should be aware of, in other words. The blockbuster strategy's continuing importance to the success of entertainment companies is made abundantly clear in the enormous amounts of data that online channels generate.

Armed with an understanding of the ways in which digital technology is transforming the markets for entertainment goods, one can easily see why YouTube has struggled to turn its immense popularity into a lucrative and sustainable business, and one can begin to make sense of parent company Google's push into Original Channels. It also becomes evident that NBC's decision to co-fund Hulu, a site focused on offering premium, professionally produced online video, may have been one of the broadcaster's smartest moves in recent years—Zucker deserves some credit for that. (Yes, it may come as a surprise, but this is not one of those black-and-white, heroes-and-villains books. Most entertainment executives have their fair share of successes and failures, and Zucker is no different.) These same underlying principles even help us see how the innovative foray into digital distribution of New York City's Metropolitan Opera—specifically, its decision to simulcast live opera to movie theaters around the world—will affect the market for opera. One critical lesson here becomes clear: blockbusters will become more—not less—relevant to popular culture, and blockbuster strategies will thrive.

A second question triggered by the emergence of online channels is whether these channels will ultimately undercut the role of established content producers and distributors. British band Radiohead made a splash a few years ago with an album they self-released, without the help of a record label or retailer, prompting many industry observers to suggest that other bands could and should release their work on their own, too. Previously unheralded musicians have on occasion developed vast fan bases on YouTube and through social networks, and some self-publishing authors have created huge demand for their writings online. As digital technologies become ever more sophisticated and ubiquitous, will creative talent increasingly seize the opportunity to market their creations directly to consumers? If so, the demise of many established entertainment companies may not be far off. According to my research, however, such an extreme scenario is unlikely: it's virtually impossible for most creative people to thrive without the benefits that these enterprises provide. Still, the rise of do-it-yourself production and distribution raises critical issues for even the largest entertainment businesses.

We can learn a lot from content creators and owners who have used digital channels to deliver their content directly to the consumer. Hulu—co-owned by NBC Universal, News Corp.'s FOX, and Disney's ABC—is an example here, too. But the world of sports has perhaps made even bigger waves. Major League Baseball's digital arm stands out: MLB's executives have embraced the opportunities that digital channels afford the league to interact directly with its fans, scoring with products for a host of different platforms and operating systems. The National Football League has taken a strikingly different approach to digital media, but its strategy has proven just as successful, and the resulting lessons for how markets for entertainment goods are evolving are remarkably consistent. All three cases—Hulu, MLB, and the NFL—show how content producers can use new digital distribution channels to their advantage. And all three again underline the benefits that blockbusters provide in that context.

None of this is to deny how disruptive the advances in technology can be to the world of entertainment. Piracy, fueled by the

same low costs of reproduction and distribution that explain digital technology's other effects, is often seen as the main culprit. But other forces—such as consumers' expectations that prices will inevitably come down in digital channels—may be more threatening. The so-called unbundling of goods in digital channels also causes headaches for entertainment businesses. For example, now that all the songs on an album are made available for individual purchase online, the album bundle is increasingly playing second fiddle to the individual song. This inversion was unthinkable in a fully analog world, if only because the costs of separately packaging and shipping songs were prohibitive. Meanwhile, the rise of massive online retailers and content aggregators with ultrathin margins has also put tremendous pressure on entertainment companies' business models.

As a result of all these tumultuous changes, blockbuster strategies will undoubtedly evolve—and what is fascinating is that some superstars seem to be leading the way. In 2010, in an award-winning campaign dreamed up by advertising agency Droga5, hip-hop mogul Jay-Z and his manager explored a partnership with Microsoft for the launch of his memoir, *Decoded*. A year later, Lady Gaga, never afraid to innovate, redefined the concept of a major launch with her *Born This Way* album. In the years to come, many more entertainers will surely follow in their footsteps. That's not a blind guess—as we'll see, it is a logical conclusion if one considers both the disruptive effects of digital technology and the factors that explain the effectiveness of blockbuster bets. Blockbuster strategies may become more difficult to execute in a digital world, but, as counterintuitive as it may sound, their relevance only increases. The future of blockbusters in the entertainment economy shines bright.

And, in fact, blockbuster strategies may increasingly pervade other sectors of the economy, along with other marketing practices borrowed from the world of entertainment. So, to conclude the road map of what's to come, I will end the book by pointing to particularly noteworthy examples I have come across in my research over the years. The nightlife business is a focus here: two of the sector's most successful impresarios are leading a revolution, transforming the business from one that is all about selling bottles—high-priced alcohol delivered to "table customers" seated at hot spots in the club—to one that is just as much about selling tickets to heavily marketed events featuring superstar DJs. But I'll also point to other examples, from Apple and its big bets in consumer electronics, to Victoria's Secret with its angelic-superstar-studded fashion shows, and to Burberry's success in taking the trench coat digital. As these will show, many of the lessons to be learned about blockbusters not only apply across the entertainment industry—they even extend to the business world at large.

Chapter One

BETTING ON BLOCKBUSTERS

In June 2012, less than two weeks after the news of his appointment as chairman of Walt Disney Pictures had Hollywood insiders buzzing, Alan Horn walked onto the Disney studio lot. The well-liked sixty-nine-year-old executive ("I try to be a nice person almost all the time, but next to Alan Horn I look like a complete jerk," actor Steve Carell had joked during Horn's good-bye party at Warner Bros.) was excited about joining Disney, which he described as "one of the most iconic and beloved entertainment companies in the world." But he also knew he had his work cut out for him, as Disney Pictures had posted disappointing box-office results in recent years. In his new role, Horn would oversee production, distribution, and marketing of live-action and animated films from Disney as well as its units Pixar Animation Studios and Marvel. Horn would have to decide whether the event-film strategy he had pioneered at Warner was the right approach for his new employer as well.

After working for producer Norman Lear early in his career and spending a decade at the helm of Castle Rock Entertainment (a production firm he had co-founded that was known for creating the hit television show *Seinfeld* and films such as *A Few Good Men*, *The Shawshank Redemption*, and *When Harry Met Sally*), Horn had moved to Warner and fostered a different attitude toward risk. "Other studios made big movies, but no one was doing this on a consistent basis," he told me. "In fact, they were afraid of it. Because the price for movie tickets was fixed, taking on higher costs seemed a bigger risk."

Described as "a consensus builder," Horn went to great lengths to ensure that his Warner colleagues embraced the event-film strategy. His first event-film pick was *The Perfect Storm*, released in 2000. "George Clooney was not a big star at the time, and neither was Mark Wahlberg, but I really liked the story," Horn recalled. "We wanted to create the best visual experience for audiences, and we spent a lot to showcase those in our marketing campaign. I remember I saw an early cut of the trailer and asked, 'Where is the storm?' I wanted a shot of the boat in the storm, with the high seas. It took half a million dollars, but they made it happen in a week. We wanted everyone to know this was going to be big. So we had to have that shot."

Within a few years, the event-film strategy had taken hold, and Warner was releasing four or five such movies annually. Horn focused on what he called "four-quadrant movies": films appealing to young and old as well as male and female moviegoers. In 2008, the studio's picks included *The Dark Knight*, *Get Smart*, *Speed Racer*, and, before its release date was moved to 2009, *Harry Potter and the Half-Blood Prince*. In 2010, Horn's last full year in charge, *Inception*, *Clash of the Titans*, and *Harry Potter and the Deathly Hallows: Part 1* were among the event films. Each event movie received a higher-than-average production and marketing budget and generally had its release date planned years in advance. "The potential upside for our event films is so enormous that we believed it was worth the risk," declared Horn.

The results proved the wisdom of his strategy: under Horn's twelve-year leadership, Warner Bros. Pictures, the largest of the six major Hollywood studios, became the first studio in history to collect more than $1 billion in theatrical revenues for ten years in a row. In 2010, the studio was the market leader in films with worldwide box-office revenues of $4.8 billion—its biggest haul ever. The eight Harry Potter films, the most successful motion picture franchise in history, collected $7.7 billion at the worldwide box office. Warner Bros.' output during this period also included several other lucrative films, including *300*, *The Dark Knight*, *The Departed*, *Gran Torino*, *The Hangover* and its sequel, *I Am Legend*, *Million Dollar Baby*, *Ocean's 11*, *12*, and *13*, and *Sherlock Holmes*.

But Horn's strategy remained controversial precisely because it seemed so risky. "Making monster projects into profit centers is no slam-dunk," wrote one *Wall Street Journal* reporter, expressing a sentiment that was widely shared. "Someday soon, one of these big bets will crash so hard that a studio will be left with a staggering write-off." Disney's own *John Carter* was a recent case in point: it had cost an estimated $250 million to produce and likely lost almost as much, easily making it 2012's biggest flop. Detractors of event-film strategies also loved to point to the western *Heaven's Gate*, otherwise known as "the film that sank a studio." Delayed for months and beset by cost overruns, the 1980 movie cost a then-unprecedented $40 million, only to be roundly rejected by both the press and the public (one influential critic called it "an unqualified disaster"). United Artists sold only $3 million's worth of tickets; as a direct result of the massive box-office flop, the studio collapsed and was sold off to MGM.

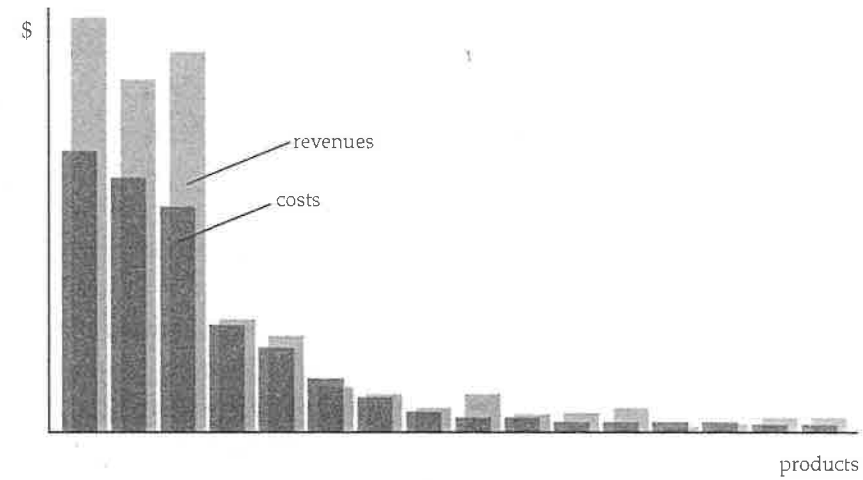
Horn acknowledged the downside of his approach. "The problem with event movies is that when we fail, it is a colossal failure." And for all of his successes, Horn also had his share of misses during his long tenure at Warner Bros. "In a good year, a major studio is happy to bat .500," he said. "The real goal is overall profitability." The countless variables involved in the moviemaking process plagued every live-action project he decided on. "When Jo Rowling was selling Harry Potter, she was turned down by a number of publishing companies. And they were reading it in the medium in which it would be released! Making a movie is—it's just ridiculous. We are reading a screenplay, and have to imagine what it will look like with a certain director, a certain cinematography, and a certain cast. You say, 'With Channing Tatum it will look this way, but if we go with Matt Damon it will look a different way.' It is such a gut-level decision that it is impossible to define criteria that can make a studio successful year in, year out."

Now, with his arrival at Disney, all eyes were on Horn to do just that: achieve success year in, year out. It didn't help that Disney's appetite for big risks was low after the *John Carter* debacle; making matters worse, Horn knew he would have to compete head-on with Warner and the very strategy he had invented. "Other Hollywood studios have embraced the event-film strategy, too," he said. "So the competition from other major studios for the best ideas, creative talent, and release dates has only increased in recent years. We will have to go up against other big movies in our release weekends." Could Horn bring the magic back to the Mouse House?

Is the event-film strategy—or, as I called it earlier, the "blockbuster strategy"—really the best approach to making and marketing entertainment? For major studios like Warner Bros. and for other large-scale content producers across the different sectors of the entertainment industry, the answer is an unequivocal "yes." In fact, the strategy that Warner Bros. followed is now a common approach among not just movie studios, but also publishers, television production companies, music labels, video game publishers, and producers in other sectors of the media and entertainment industry. But before we delve into the explanation for why such a seemingly risky approach makes sense even in today's competitive marketplace, let's take a closer look at the approach taken by Horn at Warner Bros. and understand the returns that are associated with it.

Rather than dividing its resources evenly across the products in its portfolio, a movie studio following a blockbuster strategy allocates a disproportionately large share of its production and marketing dollars to a small subset of products in the hope that they will bring in the lion's share of revenues and profits. This idea is illustrated in the chart that follows. Even amid considerable uncertainty, the studio bets heavily on the most likely hits. It makes

A Typical Pattern of Blockbuster Investments and Outcomes



"blockbuster bets": big-budget productions aimed at mass audiences. Given the nature of the movie-production process—where the trajectory from acquiring a script or the rights to a property to finally releasing a movie can easily take four years—the studio has to make its picks of the most likely winners at a very early stage. Given the fickle taste of consumers, and given the complexities of a production process that often involves hundreds of people, that's not a simple task. But, the studio's thinking goes, the rewards will be worth the risk.

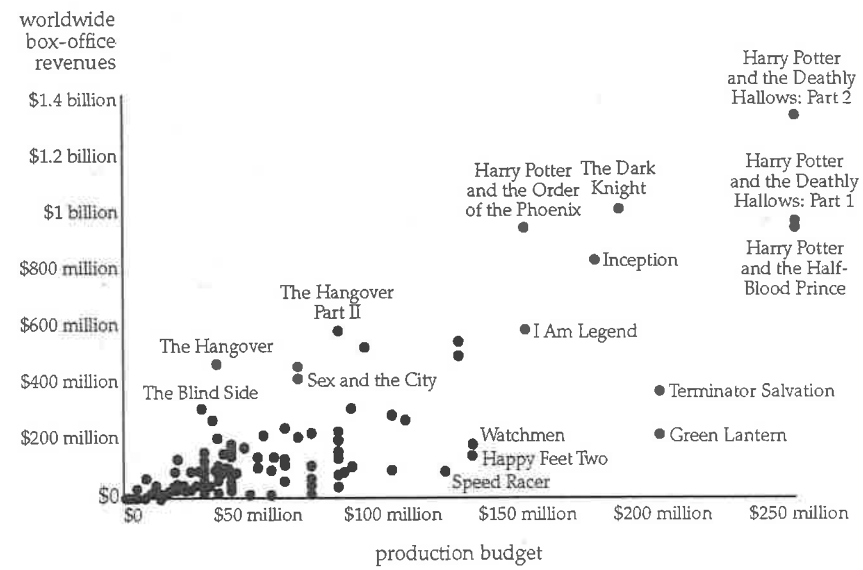
As a way of examining Warner Bros.' strategy, let's take a look at the year 2010. The studio released twenty-two films that year, spending about $1.5 billion in production costs and upward of $700 million on advertising and other promotional efforts domestically. Warner spent a third of its 2010 production budget on its three biggest titles—$250 million on *Harry Potter and the Deathly Hallows: Part 1*, $175 million on *Inception*, and $125 million on *Clash of the Titans*. Its fourth-biggest investment, the *Sex and the City* sequel, cost another $100 million. Such big bets often feature not only A-list talent but also elaborate visual effects—spectacular sequences, sweeping shots, large-scale sets, multiple locations, and high-tech stunts, for instance—all of which drive up the picture's costs. If the movie is based on a successful property such as a book or a character (as the biggest bets, such as *Harry Potter*, often are), intellectual property rights can also be costly.

"We have made a conscious decision at Warner Bros. to make four to five movies each year that have a shot at reaching $1 billion in revenues," one Warner executive said about the studio's strategy. "And if you commit a large share of your production resources to these few movies, it has implications for your other movies," Horn explained. "You might make a $60 million movie instead of a $90 million movie. It is a balancing act." A television executive I talked to made essentially the same point. "People are under the mistaken impression that studios and networks love all their children equally," he said. "But because there is only a finite amount of production and marketing money available, they have to prioritize."

At Warner Bros. under Alan Horn, the expectation was that those movies with the highest costs would also be the titles with the highest revenues—and the highest profits. In 2010, Warner's results lived up to that expectation. Although the top three biggest bets only accounted for a third of the total production budget, they were responsible for over 40 percent of the domestic and 50 percent of the worldwide box-office revenues generated that year. If we calculate the difference between production expenditures and box-office revenues, it becomes clear that over 60 percent of the year's total surplus came from the studio's top three investments, and nearly 70 percent from its top four movies. At the other extreme, the four least expensive movies released in 2010—*Flipped*, *Lottery Ticket*, *The Losers*, and *Splice*—accounted for just under 6 percent of total production spending but only 4 percent of domestic and 1 percent of foreign ticket sales, adding next to nothing to the surplus. Not all of this surplus is profit, of course—for instance, studios like Warner Bros. share close to half of their revenues with the theaters that screen their movies. But the pattern is clear: Warner's biggest investments in 2010 delivered the biggest returns.

So far, so good. But was 2010 just a lucky year, one that happened to be short of one or two big flops that could have seriously

Warner's Movie Bets from 2007 through 2011



The figure plots each of the 119 films that Warner released from 2007 through 2011 (according to research firm Rentrak) by its estimated production budget and worldwide theatrical revenues. For instance, the movie *The Hangover* cost an estimated $35 million to produce and yielded close to $470 million in ticket sales (of which $190 million came in foreign markets).

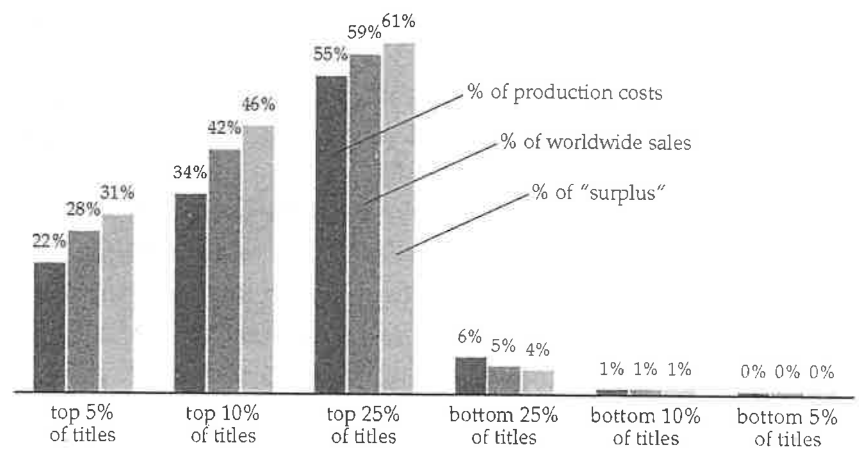
altered the picture? Are studios like Warner Bros. taking too much risk with their blockbuster bets? The performance of Warner's movies over a longer time horizon certainly does not suggest that to be the case. In fact, the 2010 results reflect a more general phenomenon. Consider the chart above, which shows the returns on Warner's bets from 2007 through 2011, the last five full years of Horn's tenure. During this period, Horn was running his tent-pole strategy at full force, spending $6.5 billion in production costs. But he was also facing strong competition from rival studios that were following his lead with big bets of their own.

At first glance, the chart may look like a random scattering of data points. The messiness of the data reflects the unpredictability of the demand for theatrical films. Warner made substantial investments in a number of well-known franchises, including Harry Potter and the Batman film *The Dark Knight*. While several of those were highly successful, other big bets stumbled at the box office—in particular, the $120 million *Speed Racer* was an unmitigated disaster. (Inspired by a Japanese anime series, starring Emile Hirsch, and released in 2008, it sold well shy of $100 million's worth of tickets across the globe.) As for the smaller investments, they seemed to present the same mix of hits, also-rans, and outright flops. *The Blind Side, The Hangover,* and *Gran Torino,* each costing less than $40 million to produce, all made a killing at the box office, while the equally affordable *The Assassination of Jesse James, Whiteout,* and *Shorts* never connected with audiences.

But take a look at the next chart, which groups films more systematically by their production budgets. Across all films released over a five-year period, the top 5 percent of films accounted for one-fifth of the total production costs and more than one-quarter of worldwide grosses. The top 10 percent of films consumed roughly a third of the costs but generated more than two-fifths of all revenues—and accounted for nearly half of the difference between production costs and revenues. Warner's biggest investments thus generated disproportionately high returns. On the other end of the spectrum, although they sometimes posted big numbers, smaller investments had little effect on the grand scheme of things. Although the bottom 25 percent of films ranked by their budget (a group that consists of movies made for just below $30 million) accounted for just 6 percent of costs, they generated only 5 percent of ticket sales. And the bottom 10 percent of movies had virtually no impact on sales.

The differences between films at both ends of Warner's portfolio may seem small in relative terms, but they are huge in absolute terms. And in the years of its biggest bets, Warner's total box-office revenues beat those of its main rivals, proving both that a blockbuster focus pays off and that individual blockbusters can significantly lift a content producer's performance. Some critics might say that Warner Bros. would have been far less successful in the mid- to late 2000s if it had not had the *Harry Potter* franchise or *The Dark Knight*. But that is exactly the point: one blockbuster bet can make a year. The best possible outcome of the blockbuster strategy

How Warner's Big Bets Stack Up Against Its Small Bets



The figure shows how much the 119 movies, when grouped by their production costs, account for Warner's production costs, worldwide box-office sales, and the difference between both (defined as "surplus"). For instance, the top 5 percent most expensive titles account for 22 percent of the production costs, 28 percent of worldwide revenues, and therefore 31 percent of the surplus.

is having a film that lifts the entire bottom line. And the way to get there, my research shows, is by making sizable investments—not by spreading the available budget across a larger number of smaller films.

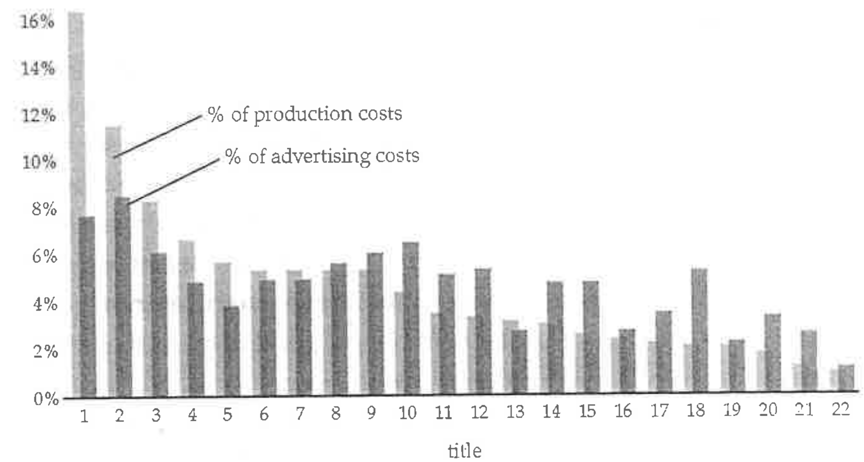
Horn's motivations for pursuing the event-film strategy are telling. "I was struck by research that shows that the average moviegoer in the US only sees five or six movies a year," he told me in 2012. "And it is even fewer in international territories. Last year, there were over 120 films released by the six major studios, and another 80 by the larger independents such as Summit and The Weinstein Company—that's hundreds of motion-picture viewing opportunities. There is a tough selection process going on," he said. "That is why having something compelling is so important—something of high production value, be it because of the story, or the stars involved, or the special visual effects." The goal, in other words, is to stand out from the competition—to win the battle for attention. That is what the blockbuster strategy is designed to do. "Even the most die-hard fans will not see more than a movie a week," Horn declared. "You have to make sure it is your movie they see."

The success of the blockbuster strategy is even more apparent when marketing costs are included. Making bigger bets results in advertising efficiencies. "The advertising expenditures for a movie that costs $150 million to make are not twice those for a $75 million movie, even if you saturate the market," Horn told me. "You need a certain amount to make sure you can support the film nationally, just to tell audiences you are out there. That makes marketing the $75 million movie expensive. But to give it the extra push you expect for an event movie is not going to cost that much more."

Although Hollywood studio executives are tight-lipped about their advertising spending, data that I obtained from an independent market research company—one that effectively counts the advertisements placed in various media (from television and newspapers to Internet and outdoors) and estimates its value—back up Horn's view. Indeed, when we look at Warner's 2010 movie slate, advertising the bigger productions was disproportionately cheap, as captured in the chart on the next page. The top three movies accounted for a third of the production budget, but those films required only 22 percent of the studio's $700-million-plus advertising budget. Promoting *Inception* ate up the highest number of advertising dollars—just over $60 million, or about a third of the movie's production costs. In contrast, Warner shelled out an extra 75 percent on top of its production budgets to advertise smaller productions like *The Town* and *Life as We Know It*, both made for less than $50 million. Once again, bigger films emerge as relatively smart investments.

With the growing importance of global markets, the relevance of blockbuster bets will only increase. "International box office results are especially strong for event movies," Horn noted. "That's where the real growth is. By 2016, the international box office is projected to be $27 billion, much larger than the domestic box office at a projected $11 billion." Because international theatrical markets are "under-screened"—meaning that when compared to the United States, other countries have relatively few theaters to serve moviegoers—international markets tend to be more selective. "They want four-quadrant movies, and they want stars or characters such as Harry Potter that they know," said Horn. "Those are the movies that travel well."

Production and Advertising Spending: Why Warner's Big Bets Pay Off More



The figure shows, for Warner's 2010 movie slate, how much each title received of Warner's total production and advertising budget. For instance, the second-most-expensive movie released in 2010, *Inception*, used 12 percent of the production budget but only 8 percent of the advertising budget. Ranked number 18 on the list with 2 percent of the production budget, the movie *Cop Out* received as much as 5 percent of the advertising budget.

Movies make much of their revenues outside theaters—from such sources as DVD sales and rentals, streaming rentals, and television—which in theory is a way for smaller movies to make up for the lackluster returns. But in reality, the best predictor of a movie's revenues in subsequent distribution channels (or "windows") is its performance in the theatrical window. "All the ancillary markets are driven by theatrical," Horn said. "The revenues from DVD sales are almost directly proportional to box-office revenues. So those ancillary markets do not bail the smaller movies out." In fact, when taking into account those other sources of revenues, the effect of bigger investments generating a better payoff is only magnified.

Properly executing a blockbuster strategy is more than just a matter of spending more money in order to generate higher revenues, of course—if the game were really that simple, anyone with deep pockets could be a successful studio head. Instead, it is about making the right bets. "There is no hope if you just make a bad movie," Horn declared. "You can try everything you want with your release strategy, but if the movie is not good enough, you are done. You have to have a good idea, and execute it well."

Luck helps as well. Warner Bros. had heaps of it with its biggest blockbuster, *Harry Potter*, as illustrated by the story of how Warner came to acquire the rights. "We had the rights to *Harry Potter* even before the book was a success in the UK," Horn told me. "A woman in the UK happened to buy the book in a store one day, as a gift for a family member. She liked it so much that she showed it to her boss, David Heyman, whom she worked for as an assistant, saying 'You have to read this—this is brilliant.' Now get this: David had a production deal with Warner Bros. And one of his childhood friends, Lionel Wigram, was an executive with us. So he pushed us to option it. But nobody knew what they had until the book exploded, and off we went." Warner's good fortune did not stop there, Horn recalled: "Before the book became known, my predecessor offered the *Harry Potter* property to [rival studio] DreamWorks in a partnership—and they passed. And then of course it became a hit, a little rocket ship that was taking off, and they called back and said, 'This was offered to us; we want to be partners with you.' But I said, 'No, you turned it down, and the offer is off the table.' I had it in writing. Now isn't that something?"

Harry Potter aside, have Horn and his team sometimes picked the wrong titles to focus their attention on? Yes. Each time one of Warner's big-budget event movies bombed, the studio incurred a substantial loss. "*Speed Racer* made a bigger dent in our bottom line

than any other movie in 2008," recalled Horn. "The Wachowski siblings wanted to make a family picture, with bright colors, giving it a cartoonish feel. It was very costly and, in the end, too big a leap. But to this day I don't fault them. It could have been the most innovative movie in history. You have to take risks." He added: "You've got to realize that someone walked into somebody's office at Pixar one day, saying they had an idea for an eighty-year-old man and a ten-year-old kid to take off in a house fueled by a balloon. You can see people go 'Wait a minute. . . .' But they made it anyway, and it was a tremendous success." (*Up* grossed well over $700 million at the box office.)

And has Horn greenlighted breakout hits that no one at the studio saw coming? Absolutely. *The Hangover*, for instance, was produced for only $35 million, but it pulled down $470 million in ticket sales, shattering every record for R-rated comedies along the way. Not surprisingly, Warner turned the sequel into a tent-pole movie, with a production and marketing budget set accordingly—this time, the studio took no chances. The same is true for *Sex and the City* and its sequel: the first movie was a small bet that performed much better than expected, and the second got the full tent-pole treatment.

The blockbuster strategy is certainly not risk free, and there are limits as to how much studios can spend on any given film. But what is critical to understand is that a studio would be taking a *greater* risk if it put more emphasis on movies with lower production budgets—if, effectively, it made a larger number of smaller bets. It may sound counterintuitive, but for a studio like Warner Bros. those smaller bets could, in a typical year, actually lose the studio more money than they bring in. Even if some smaller investments do make money, a dollar spent on a big-budget film will average a much higher profit.

Another film studio, Paramount, learned these lessons the hard way—much as NBC did. In the late 1990s, Paramount chose to steer away from what its management saw as a dangerous reliance on big bets. It adopted a philosophy of sticking to mid-range budgets and lesser-known stars, and boasted that it would run its movie production slate "like an actuary chart." But while the mantra on the studio lot was protecting the downside, the studio's cautious strategy ultimately had the opposite effect: by early 2004, Paramount had become known for mostly B-grade films featuring mediocre talent, and its profits had fallen by more than 30 percent. Realizing what was happening, Paramount's executives promptly reversed course, letting the creative community know that the studio was once again willing to pay top dollar for its movies, in part by giving Adam Sandler, Charlize Theron, and other top actors their highest salaries to date to star in upcoming movies. "We intend to relax risk aversion policies and to make more money available to finance more challenging productions," said Sumner Redstone, chairman of Paramount's parent company Viacom, at the time.

Only a mighty studio with significant scale and resources can aggressively pursue a blockbuster strategy—after all, it must be able to absorb an occasional loss the size of a *Speed Racer* or *The Adventures of Pluto Nash*. (The latter was one of the biggest box-office disasters of all time, costing a reported $100 million to produce but generating only $4 million in US theaters in 2002.) Like Warner Bros., Disney's film studio has the resources to invest in blockbusters. So don't expect the studio to dial back its bets on big movies under Horn's leadership.

Some of the reasons why the cost of making movies can run into the hundreds of millions of dollars are easy to understand, but other investments may be more difficult to comprehend. Film studios or television networks paying an actor or actress millions of dollars based on a hunch that audiences will want to see that person star in a movie or show, for instance, especially when there is no shortage of people waiting for their shot to make it in show business. Or producers investing heavily in an untested script just because the subject matter, be it superheroes or vampires, is "hot." Can't entertainment companies consistently avoid such enormous expenses? To find the answer, it's useful to consider why entertainment executives often get caught up in bidding wars. One of the most daring bids in the world of book publishing may be a good place to start.

His charming, unassuming personality easily made up for it, but Dewey Readmore Books, the star of Vicki Myron's *Dewey: The Small-Town Library Cat Who Touched the World*, was one fat cat. A million-dollar cat, in fact. In 2007, the Manhattan-based publishing house Grand Central Publishing shelled out $1.25 million for the rights to the book about the fluffy orange creature, found abandoned as a kitten in the returned-book slot of the Iowa public library in which Myron worked.

Five days before the publisher made the winning bid, Karen Kosztolnyik, then a senior editor at Grand Central Publishing, received a forty-five-page book proposal from Myron's literary agent, Peter McGuigan. Impressed by what she read, Kosztolnyik quickly passed the document on to her boss, Jamie Raab, then senior vice president and publisher of Grand Central, who was hooked on *Dewey* just two pages into the proposal. The following day, they started the bidding process by offering an advance of $300,000, already a significant amount for a book by a first-time author. Author advances in the tens of thousands of dollars were much more common. (Such advances are payments made against an author's royalty, which usually run between 10 percent and 15 percent of the retail price of a hardcover book.) A frantic bidding war ensued, during which McGuigan told Kosztolnyik that a second publisher was shadowing Grand Central's every move. But Raab urged Kosztolnyik to "do everything humanly possible to buy this book," and Grand Central eventually acquired the book in a preemptive strike, a day ahead of a scheduled auction that would have involved other publishers.

Raab and Kosztolnyik had high hopes for *Dewey*, billed as the feline answer to the best-selling *Marley & Me: Life and Love with the World's Worst Dog*, John Grogan's 2005 memoir of his misbehaving Labrador retriever. *Marley & Me* had garnered critical and commercial success, selling over three million copies to date. Dewey was no stranger to the spotlight. Over the course of his nineteen-year life, this unusually resilient cat—named in a contest after the

Dewey Decimal System used in most libraries to catalog books—became a mascot for the library and the town of Spencer, Iowa. As his popularity grew, he even started to attract the attention of tourists and filmmakers, appearing in two documentary films. Shortly after he died in November 2006—in Vicki Myron's arms—his obituary ran in more than 250 publications, including *USA Today* and the *Washington Post*.

However, this was an unprecedented level of pressure even for *Dewey*. When that exceedingly high bid was tendered, the reaction in many quarters was disbelief. William Morrow, a HarperCollins imprint, had paid a mere $200,000 for the rights to *Marley & Me* back in 2004. Grand Central's gamble on *Dewey* immediately turned the book into one of the publisher's biggest bets for the year among its annual output of 275 to 300 books. "It's stunning, the advances being paid. If it might be the next *Da Vinci Code* or the next *Marley & Me*, the ante just increases, " Robert Miller, the president of rival publisher Hyperion, said. The proposal did not scream instant success: typically, cat books are not big sellers. According to Kosztolnyik's records, Peter Gethers's *The Cat Who Went to Paris* and Stephen Baker's *How to Live with a Neurotic Cat*—next to *Marley & Me* the two most comparable titles—had sold only around 30,000 and 120,000 paperback units, respectively. And the book's main character had died—making him unavailable for, say, a publicity-grabbing appearance on Oprah Winfrey's couch.

"Magical things always happen around Dewey," Myron said about her furry friend after the bidding. But with more than a year until the book was published, it would be a while before Grand Central learned whether its seemingly outrageous bid for the manuscript had been the right move.

The double-or-nothing daring move to acquire *Dewey* was only one in a string of big bets made by Grand Central and a host of other leading publishing houses. Like major Hollywood studios, book publishers, too, have largely adopted a blockbuster strategy. In the year before the *Dewey* gamble, for instance, Grand Central spent close to 20 percent of its total adult hardcover acquisition

budget of $40 million on its biggest title alone, and over half of this budget on the five most expensive titles on its list of roughly sixty adult hardcover front-list titles. (A publisher's front list is its catalog of new books; its back list contains books that have already appeared in an initial edition. On average, about 70 percent to 75 percent of a major publisher's sales comes from front-list titles.) Grand Central chose to compete this way in a sector where, like the film industry, the failure rate is high: only about one of every five new books recovers its costs in the marketplace, and retailers reportedly return roughly 30 percent of all publishers' physical book shipments. While exact rates differ across the various sectors and genres, it generally is the case that, for any given title, the most probable outcome is a financial loss.

Grand Central's aggressive pursuit of *Dewey* may prompt a prudent manager in any other industry to wonder what on earth the company was thinking. Faced with such low odds of success, why would Grand Central put itself in the position of having to outsell all cat books released in recent memory to earn back its seven-figure advance and make a decent profit? Rather than putting all their eggs in one basket, wouldn't the executives at Grand Central be smarter to place a larger number of smaller bets on a range of topics or, if the belief in pet books is so strong, commission a number of books on feline or other creatures? Publishers, like movie studios and other entertainment companies, sometimes seem like riverboat gamblers. What explains the prevalence of audacious bets such as the one Grand Central placed on *Dewey*?

The first thing to understand is that, given the variability in execution of books, movies, and television series, and given the constantly shifting tastes of consumers, it is extremely difficult to forecast demand for any individual new title. Speaking about the movie business, screenwriter William Goldman once said, "Nobody knows anything." Executives in the film industry often quote that famous line, and although it may be too strong a statement, Goldman's words accurately reflect the frustration of having to make a prediction based on just a proposal, a script, or even a pilot.

"It *is* guesswork," Jamie Raab told me. "To some extent, we are all just winging it. I have a good track record of picking winners, but it is far from perfect. No one in this industry has a perfect score. It really is a crapshoot, albeit an 'informed' crapshoot." The one useful indicator of potential—and this is a critical notion that drives much of how entertainment industries operate—is a new idea's resemblance along some dimension to an existing hit. But that is an indicator that, by its nature, is evident to any industry player, so there is heavy convergence of interest on certain properties. This, in turn, triggers competitive bidding situations for proposals and soaring fees for the creative people who can bring these properties to the page, the big or small screen, or indeed to any mass entertainment medium.

This was the kind of luck that *Dewey*, in characteristic fashion, stepped into. Soon after the book proposal started to make the rounds, many industry insiders compared *Dewey* to the runaway hit *Marley & Me*. The sixth-highest-selling book (fiction or nonfiction) of 2006, it spawned two related children's titles also written by Grogan about his rambunctious canine (an adaptation for ages eight to twelve, *Marley: A Dog Like No Other*, and the new adventure *Bad Dog, Marley!*), a number of other dog books, and even a Hollywood movie starring Jennifer Aniston and Owen Wilson. Publishers saw essential similarities in Dewey's story: it was a touching story about how an animal could bring out the humanity in people it encountered, featuring an animal that was much more than just an average pet. It would surely appeal to pet lovers, many felt.

While executives at Grand Central were careful about making comparisons between *Dewey* and *Marley*—the world is divided into cat and dog lovers, after all, and every title needs to be judged on its own merits—the similarities undeniably spurred publishers' enthusiasm for the *Dewey* rights. Fearful that the price would reach astronomical heights at auction, Grand Central snapped up the book a day before several other publishers would have had their shot at it. "You can't underestimate the market out there for people who love animals," remarked Kosztolnyik, who would oversee the editorial process. "*Marley & Me* has been a publishing phenomenon. I think there are equally as many cat lovers as there are dog lovers."

These same dynamics also explain why, when the popular television series *Sex and the City* ended in 2004, not one but two shows—*Lipstick Jungle* and *Cashmere Mafia*—sought to fill the gap by building a show around three successful professional women living in New York City. Likewise, the best-selling *Twilight* series sparked a renewed interest in vampires, and we have the smash hit *American Idol* to thank for the onslaught of talent shows—including NBC's *The Voice*—that fill our television screens.

During Alan Horn's tenure at Warner, many of the studio's event films were based on properties that had established their value in other domains. *Harry Potter*, for instance, was a megahit in book form, and *The Dark Knight* was based on the Batman comic-book series. Other event films leaned on formats that had worked in the past, be they sequels to original films that were a resounding success, such as *The Hangover* and *Sex and the City*, or ideas that featured stars, directors, or writers that have previously scored a hit. Even *Speed Racer* fit this pattern, remarked Horn: "The Wachowski siblings had done three *Matrix* movies which were phenomenally successful, and their next film, *V for Vendetta*, also made a fair amount of money. When they, with their track record, said they wanted to do *Speed Racer*, it was hard to say no."

When planning sequels to movie franchises or additional seasons of successful television series, studio executives will strive to leave a "winning formula" unchanged and thus avoid uncertainty about how, say, a switch of a lead actor or talent show judge will pay off. As a result, the costs of production often dramatically increase over time. *American Idol* is an example: in 2009 Simon Cowell was rumored to have pocketed well over $100 million to extend his run as a judge on the show for one more year. (He later launched *X Factor*, a rival talent show, in the United States.)

With so much money invested in their most promising projects, entertainment executives will understandably do everything in their power to make these products a success in the marketplace. For both its fall/winter and spring/summer lists, Grand Central turns a handful of its biggest bets into what Raab calls "focus books," which receive a disproportionately high level of attention and promotional dollars. Of those, a small handful of titles per season are the all-important "make" books. "We pull out all the stops to make those books happen," explained Raab. Focus books will get more attention from the marketing and sales team, more time during meetings (such as those with sales representatives), and a more prominent placement in the publisher's catalog for retailers. At Warner Bros., event films not only receive a higher production and marketing budget; they are also often slotted into the most favorable opening weekends (such as around Memorial Day in the United States), and more efforts are dedicated to these films in dealings with exhibitors, retailers, and other partners. Similarly, television networks' biggest bets are given the most valuable times in the television schedule and more airtime for promotions. The holy grail here is a spot during the Super Bowl, watched in recent years by a hundred million viewers—or, even better, airing an episode immediately after the game, as NBC chose to do in 2012 with a special episode of *The Voice*.

To pursue a more cautious strategy seems foolish. After all, if a product like *Dewey*, *The Dark Knight*, or *The Voice* fails to draw audiences, an entertainment company knows its profitability will be severely hurt. At the same time, the effect is to escalate the company's commitment and increase the size of its bet. With such high stakes and money tied up in a few big projects in the pipeline, the need to score big with a next project becomes more pressing, and the process repeats itself. The result is what I call a "blockbuster trap": a spiral of ever-increasing bets on the most promising concepts.

And so it happens that the expenditures required to procure winning properties can reach bet-the-farm proportions—this explains why NBC and Paramount were inclined to switch away from a blockbuster strategy for a time. When a first-time author can produce a bestseller like *The Art of Fielding* (a much-praised novel by Chad Harbach), when a show like *American Idol* can draw a huge audience after getting its start in an unfavorable summer slot amid decidedly modest expectations, and when a no-name

filmmaker with a minuscule budget can produce a major hit like *The Blair Witch Project* or *Paranormal Activity*, it might seem inadvisable to pay so much for material. The race for the next blockbuster can even stifle innovation: the same tendencies that lead to bidding wars for projects that resemble past winners work against other projects that look nothing like them but may have strong merits of their own. Many movie lovers lament the offerings available to them in theaters and speak disapprovingly of a market in which nine of the top ten selling movies in 2011 were sequels of major franchises, and the tenth, *Thor*, was based on a comic-book character.

Yet, as much as managers may crave to reduce the risks that go hand in hand with big bets, and as much as we might want to criticize entertainment executives for single-mindedly chasing after winning formulas, forgoing blockbuster bets altogether likely creates even more problems. What happens if a publisher like Grand Central decides to stop making large bids like the one it tendered for *Dewey*, or when a studio like Warner Bros. forgoes the kinds of investments associated with its event films? And what happens if a content producer of any kind walks away from the most sought-after, and therefore expensive, new properties?

First, when businesses opt out of the blockbuster race, they take themselves out of the market for the most promising new projects. Literary agents will stop sending their most sought-after book proposals and movie scripts to such a producer. "If you are constantly backing out of big-ticket auctions your list is going to hurt," one publishing executive told me. "You are going to get a stigma that you don't play for the big ones, and you are going to get shunned. Say historically you won't bid more than $2 million on a book, but an agent thinks they can get $10 million on a project. Why would they bother letting you into the loop? They will no longer consider you for what they feel are their best projects."

Editors at publishing houses work hard to cultivate working relationships with agents because they tend to be the sources for the lion's share of proposals that eventually are turned into books. Even if a publisher could develop extraordinary competence in finding gold in the "slush pile" of thousands of pieces of unsolicited material received each year from aspiring authors, the dividends would be limited. After one success, the talent the publisher has nurtured would discover the value of an agent, driving up the advance needed to sign the writer's subsequent books. The same need to build relationships and be "in the market" for the best projects exists in the film business. "Sometimes this industry is like the mafia—it's about showing respect," said one Warner Bros. executive. Similarly, if a television network starts "managing for margins" rather than aiming for the widest possible audience, then agents, producers, and writers may quickly stop considering that network a good destination for their best projects.

In every entertainment business, a strong lineup of projects is often key to cultivating the next hit. Consider the world of television. Viewership is "sticky": many viewers will not immediately switch channels after seeing their favorite program, meaning they may also end up watching the program in the next slot. In addition, networks primarily advertise new shows using promotions they run on their own channels, so that much of a new program's viewership is a direct result of the popularity of the other programs on its channel. Even a casual examination of television schedules over the years reveals strong success-breeds-success trends. It is no coincidence that ABC launched *Grey's Anatomy* and a number of other successes on a Sunday evening anchored by its breakout hit *Desperate Housewives*. Likewise, FOX used *American Idol* to boost *House*, *Lie to Me*, and most recently *Glee*. As a result, any smart producer sitting on what he or she believes is the next big idea in television will prefer to do business with the most popular network, as that increases the chances of market success. So the more content producers focus on saving costs rather than driving sales, the more they lose their bid to contend for the most promising new projects.

Second, if a publisher or studio would constantly shy away from blockbuster bets, the most talented editors, filmmakers, television producers, and other creative talent would leave to work for a company that would let them pursue the projects they thought

had the highest chances of success. This is not because of the much-discussed "big egos" of creative workers—a factor often named in the aftermath of bidding wars. It's a simple result of the passion that many media and entertainment professionals bring to their work—and the fact that careers are built on blockbusters. Grand Central's publisher and now president Jamie Raab, for example, is known for discovering the best-selling romance novelist Nicholas Sparks. As a result, Raab receives a steady stream of the best new love stories from literary agents.

When you work on a project-by-project basis, as most creative workers do, every project could be your last. Hits buy you extra time and new opportunities in your career. A few misses here and there can be overcome: A-list talent is rarely evaluated on a "hit rate" or "batting average"—the total number of hits, or just the most recent hit, generally matters more. George Clooney, for instance, became a leading man in the 1990s after his star turn on NBC's popular series *ER*—at the time, everyone seemed to have forgotten that he had previously played parts in more than a dozen television shows that never went anywhere. But people and projects that have "failure" written all over them often receive the cold shoulder.

When, in the mid-2000s, a brave producer named Rob Ahrens wanted to resurrect the 1980 Olivia Newton-John roller-disco film *Xanadu*—widely seen as one of Hollywood's biggest debacles ever—as a Broadway musical, he encountered strong resistance. Described by influential film critics as "the epic failure to end all epic failures," "the most dreadful, tasteless movie of the decade," and "truly stupendously bad" (one critic simply warned audiences to "Xana-don't!"), *Xanadu* is credited with inspiring the Golden Raspberry Awards, affectionately known as the "Razzies" and now an annual celebration of Hollywood's worst moviemaking. Not the most likely candidate for a musical adaptation, to say the least.

Although Broadway productions based on box-office hits are common—*Spamalot*, described by its makers as a musical "lovingly ripped off" from the successful motion picture *Monty Python and the Holy Grail*, is one example—shows based on Hollywood flops are rare. Not surprisingly, Ahrens faced numerous obstacles during his five-year quest for support. "As soon as you say *Xanadu*," he remarked, "[people] either get it right away, or they look down on you and then they call the police." When Ahrens approached Douglas Carter Beane, his choice for playwright, Beane's first response—"No! Never!"—was not encouraging. "I passed several times, because it's a really bad movie," said Beane, who initially saw the opportunity as "theater suicide wrapped up in a nice box." He added: "My partner said, 'That sounds like a resume stopper.' Another friend of mine said, 'Do you want to keep working in this business we call show?' "

Third, by extension, not bidding for sought-after projects makes it harder to get best efforts from sales and marketing representatives and other employees. After winning the hotly contested rights to a book like *Dewey*, Grand Central executives can forcefully make the case that this book will beat its competitors. ("It's a sure bet to do as well as *Marley & Me*—why else would everyone be after it?") The same principle holds true in the film industry. As Horn put it, "It's really hard to convince marketing people to get behind a project when they have nothing to sell, whether it is a big star or a well-known literary property." Firing up those who will be involved in the development and marketing process is crucial, especially because most media titles have only a short window in which to make money and the lion's share of marketing activity takes place before their launch—when it is still largely unknown how audiences will respond.

Finding and fostering internal champions of projects is an integral part of executing a blockbuster strategy. Raab described their national sales meeting, held twice a year and attended by all salespeople, as a "pep rally." As she told me, "The idea is to have everyone walk out excited. Our job is to create the conditions to make a splash in the market—to get people to buy into our hopeful thinking." Similarly, at Grand Central's launch meetings, during which the company's projects are formally introduced to internal constituents from the editorial, sales, marketing, and other departments, as well as several senior executives of Grand Central's parent company Hachette, "a smart editor will make comparisons with other successful products [so] everyone understands this is going to be a big book," as the director of marketing put it.

Fourth, critically, if entertainment businesses forgo making big bets on likely blockbusters, they will find their channel power waning over time. Retailer support is decisive in most media markets. In the film industry, the number of screens a movie receives from exhibitors in its first few weeks remains the best predictor of its revenues. Exhibitors want to see evidence that a movie is worthy of their scarce resources; they like nothing better than to know that a studio is making a significant push for a film and planning an extensive marketing campaign. A blockbuster strategy helps them to use their resources effectively. "Exhibitors totally embrace the blockbuster philosophy," said Horn. "They don't bear any of the costs—whether the movie costs $20 million or $200 million makes no difference to them. But they do see the benefits of us spending more. What they want to do is sell popcorn. Blockbuster movies put a lot more people in seats, which means they sell more popcorn. That's the beauty of it for them."

In the book business, a large share of products is bought on impulse—surveys show that just under three-quarters of the people entering a bookstore buy a book they did not intend to buy—so securing significant display space with book retailers such Barnes & Noble is particularly important. These "pile 'em high and watch 'em fly" tactics may seem old-fashioned, but they tend to be very effective at triggering sales. For television networks, getting buy-in from local television stations is crucial, and stations often strongly object to cost-cutting measures that may reduce the likely size of a popular show's audience. NBC experienced this firsthand in 2009 when the network announced that it would move Jay Leno's new show to the ten p.m. slot in place of more expensive dramatic content, which station managers believe is a better lead-in for local news programs.

The way in which retailers market entertainment products to consumers is driven by the same forces that made *Dewey* such a pricey creature. This is noticeable even in the smallest details. If you had walked into a Borders bookstore around the time of the book's launch, you might have noticed the "Like This? Try These" signs with one arrow pointing to the bestseller *Marley & Me* and another arrow to several books that were similar to that book: *The Art of Racing in the Rain*, *A Three Dog Life*, and *Merle's Door*, all books about dogs. When *Dewey* hit the shelves, it, too, claimed a spot on that row—as much a "copycat" strategy as one will ever see. And so content producers, in turn, try to cater to the marketing strategies of retailers, sometimes going so far as to copy the look of products. For instance, publishers hoping to speak to the same audience that made Malcolm Gladwell's *The Tipping Point* a huge hit sometimes mimic that book's distinctive cover design. Gladwell himself has had no reason to change his winning formula: it's no coincidence that his more recent books, *Blink* and *Outliers*, look like they belong right next to *The Tipping Point* on the shelf. Many of the biggest blockbusters spawn knockoffs and imitators: in 2012 the erotic novel *Fifty Shades of Grey* prompted the release of such titles as *Fifty Shades of Pleasure* and *The Ninety Days of Genevieve*. (Literary agent Jonny Geller joked that his agency is now seeing so many unsolicited erotica manuscripts, they have renamed the "slush pile" the "blush pile.")

New channels through which consumers buy books work in similar ways: Amazon automatically lists comparable books under the "Customers Who Bought This Item Also Bought" section, which undoubtedly helps drive sales for those titles. By the same token, new films and television programs are often described as being "from the producers that brought you . . ." to highlight similarities with past winners, and promotions and trailers are placed around current hits that resemble them in some important way, be it the story line, central property, or star actor.

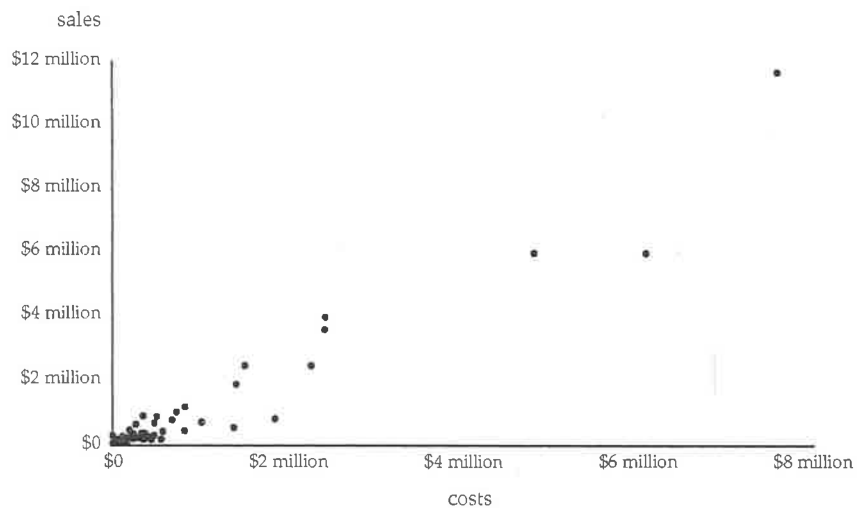
The blockbuster-focused marketing of many entertainment companies did not emerge in a vacuum—it mirrors the way consumers make choices among a wealth of competing entertainment offerings. Because people are inherently social, they generally find value in reading the same books and watching the same television shows and movies that others do. People have a taste for winners:

if, say, a book is popular and has been widely discussed in the media, consumers have more reason to read it than they would an otherwise identical book that has not received such attention. Compounding this tendency is the fact that media products are what economists call "experience goods," that is, audiences have trouble evaluating them before having consumed or experienced them. Unable to judge a book by its cover, readers look for cues as to its suitability for them. A prospective purchaser of Vicki Myron's book will thus find it very useful to hear that *Dewey* is "a *Marley & Me* for cat lovers." Just as publishers do, consumers value resemblances to past favorites.

No surprise, then, that the blockbuster strategy seemed to work wonders for Grand Central during the period *Dewey* was published, just as it did for Warner Bros. under Alan Horn. In 2006, the year before the company acquired the book, Grand Central's fall list consisted of sixty-one adult hardcover front-list titles. Just 20 percent of those titles accounted for roughly 80 percent of sales and an even larger share of profits. "The sins of the many are offset by the plentiful of the few," said one of the company's financial executives. As shown in the chart on the next page, the titles on its fall 2006 list with the highest acquisition costs were for the most part the titles that delivered the highest revenues—and the highest profits. Results are even more skewed than for Warner Bros.: the top 10 percent of Grand Central's titles account for 64 percent of its costs, 72 percent of its net sales, and a staggering 126 percent of its profits.

Remarkably, Grand Central made the lion's share of its profits on just one book—and that title was by far its most expensive. The most popular title that fall cost $7.5 million to develop and market. The book generated net sales of just under $12 million, and gross profits of nearly $5 million—out of the nearly $6 million in total gross profits across the entire list. Meanwhile, as the chart on the following page also shows, many of the publisher's small and medium-size bets lost money. For instance, the thirty titles that were cheapest to acquire actually lost an average of $12,000 each. Even the rare winners among Grand Central's least expensive books

Grand Central Publishing's Bets in 2006

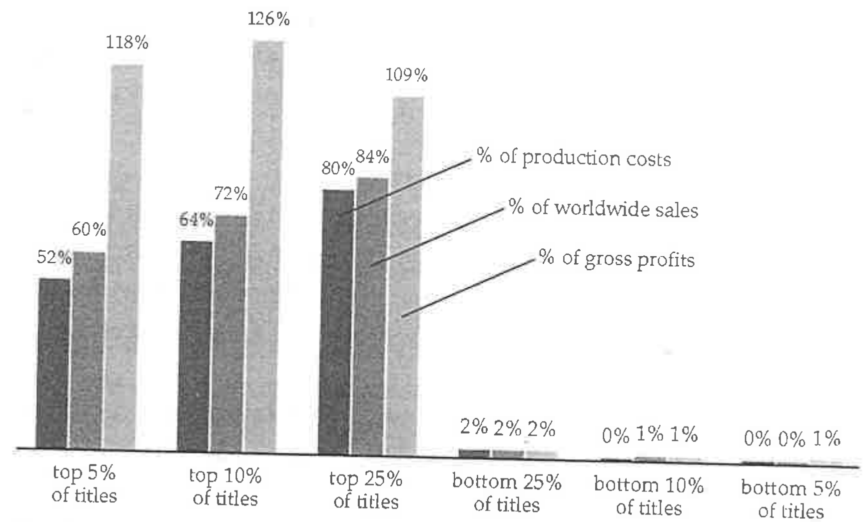


The above figure plots each of the sixty-one hardcover books on Grand Central Publishing's fall 2006 front list by its net sales and (development and marketing) costs. (The publisher asked for the titles not to be identified). The most expensive title on the list cost over $7.5 million and generated $11.6 million in net sales.

contributed very little to the company's profitability. And this particular list is no exception; it is illustrative of the publisher's results in other years as well.

As this example again makes clear, the idea of smaller bets being "safer" is a myth. Blockbuster strategies reliably beat the alternative of more risk-averse strategies: the highest-performing companies in the entertainment and media sector thrive by investing a relatively large proportion of their resources in just a few titles and then turning those choices into successes by giving them a higher level of development and marketing support. It may be partly a self-fulfilling prophecy, but it works. And because the marginal cost of reproducing and distributing entertainment products is relatively low—especially compared to their up-front production expenses—and because of the economies of scale involved in advertising campaigns, the advantage of a bestseller, a box-office champion, or a ratings monster is huge.

How Grand Central's Big Bets Stack Up Against Its Small Bets



The figure shows how much the fall 2006 hardcover titles, when grouped by their costs, contribute to the publisher's total costs, net sales, and gross profits. For instance, the top 5 percent, the most expensive titles, account for just over half of the development and marketing costs, 60 percent of net sales, and 118 percent of gross profits.

This does not mean media companies can spend without limits, of course—especially given the turbulent markets for their products. Book publishers are experiencing uncertain times with the rise of e-books, broadcast networks see their market shrinking relative to premium cable channels, and film studios can no longer count on DVD sales to be the dependable cash cow they once were. But yielding to an excess of caution and shying away from any attempt to create the next blockbuster with mass appeal may be the surest way for an entertainment company to lose further ground.

As for *Dewey*, how did our fat-cat friend fare? Published in September 2008, the book became one of those blockbuster bets that paid off—and then some. Released at a list price of $19.99, Grand Central's big gamble performed beyond any of the executives' wildest dreams. It captured the number one spot on the *New York Times* hardcover bestseller list and sold 759,000 copies in just over three months, making it the sixth-highest-selling adult nonfiction title that year. It sold another 130,000 hardcover copies in 2009, bringing the total close to 900,000 copies. Having tasted success with cat books, that same year another Hachette imprint published a children's book by Vicki Myron, Bret Witter, and illustrator Steve James. Called *Dewey: There's a Cat in the Library*, it sold 106,000 copies. The next year, Myron and Witter launched another follow-up, *Dewey's Nine Lives: The Legacy of the Small-Town Library Cat Who Inspired Millions*, which offered "nine funny, inspiring, and heartwarming stories about cats." At one point, there was even talk of a movie adaptation starring Meryl Streep as Dewey's caretaker.

Perhaps the key question is not why entertainment executives make blockbuster bets—the real puzzle, it seems, is why they continue to turn out products that are the result of much smaller bets. After all, the financial payoff from these modest investments looks decidedly shaky. If tent-pole films consistently generate the highest returns for Warner Bros., why does the studio also invest in the smaller films that make up the large majority of its annual output? And if Grand Central's expensive "focus" and "make" books consistently outperform the large majority of other titles on its list, why even bother with those smaller investments?

A close look at the way successful entertainment companies operate reveals that both kinds of investments play an important role in their portfolios. Bigger bets tend to generate the highest revenues and profits, bring excitement to the company, help build the brand, and foster future hits. But for a book publisher, a film or television studio, or another type of media producer to carry out a blockbuster strategy, smaller bets are needed, too—for a variety of reasons.

First, smaller investments can serve as test cases. Placing a reasonable number of less expensive bets can help a media producer discover the next big-hit franchise. In the film industry, sequels are seen as one the safest blockbuster bets one can make, and smaller investments may help turn up another film that is ripe for a sequel, much like *The Hangover* and *Sex and the City*. This principle also applies to actors, directors, and other creative workers. Even if studio

executives are convinced that a little-known actor is the next Tom Cruise, asking him to star in a $200 million film in his very first assignment seems ill advised. Instead, it is more sensible to commence a collaboration with a promising young actor by giving him a role in a smaller film, one that will allow the studio to learn whether he is truly capable of "carrying a film" and accomplishing all that comes with that responsibility, from performing at a high level on the set every day to fulfilling publicity obligations. Being able to test the appeal of new product formats, from vampire movies to talent shows, is another advantage. Some product types or genres may prove profitable as smaller-scope investments in their own right, as seems to be the case, for instance, with certain ultra-low-budget horror films.

Smaller bets can also help a media producer "fill the pipeline," thereby keeping companies that help sell the producer's output satisfied. For example, a book publisher that delivers a steady stream of new titles to the market will find it easier to build and maintain relationships with retailers. That, in turn, may put the publisher in a position to negotiate steeper discounts, favorable in-store placements, or other marketing advantages. In the film industry, Warner's commitment to producing two dozen movies each year—roughly one Warner Bros. film opens in theaters every other week—helps it to obtain better agreements with theater owners. "Our head of domestic distribution would go out and speak with exhibitors and say, 'I need your best theater on Wilshire Boulevard and I need it for four weeks,'" Horn told me. "The exhibitor might counter that Paramount wants it, too. But then we could say, 'We are Warner Bros., here is our lineup for the year, and this is what we need for this particular movie.' It will always be a back-and-forth in these negotiations, but having the largest number of films gave us weight in the marketplace, which got us better screens, for a longer time, and at a better revenue-sharing rate." Additionally, a larger number of products often leads to volume discounts in media buys: the more products they advertise, the more favorable the advertising rates studios and publishers can secure.

Pursuing a wide range of smaller projects allows studios, publishers, and other entertainment businesses to form closer links with agents, who are involved in the lion's share of deals for new products and therefore critical gatekeepers in virtually any entertainment sector. Further, a broad portfolio of properties can attract needed financing. For a studio like Warner Bros., which under Horn's leadership relied on co-financing for nearly all of its projects but the surest bets like *Harry Potter*, a broad portfolio can be a useful way to attract outside investors willing to share risk. The studio takes a distribution fee off the top, and then splits revenues with those investors. "Some investors may push back on this model, but they usually don't have the power and the relationships to be an effective distributor, so we have the upper hand in these talks," said Horn. "Again, our scale worked in our favor."

That smaller bets may allow for more flexibility in dealing with these industry partners is an added advantage. For example, it is often easier to move release dates and shift advertising budgets for smaller-scale projects. Large media producers may buy advertising time on television months in advance; having smaller projects to move around can help optimize the use of those resources.

Going for smaller-scale products can enable entertainment companies to build and maintain a favorable critical reputation as well, which in turn can help them attract sought-after A-list talent and their projects. If, say, a film studio wants to cast a superstar actor in an event film, it can be beneficial to have the option of offering that actor the lead in a smaller "passion project," one with the potential to please critics and Academy Award voters. When Warner Bros. agreed to finance Clint Eastwood's *Million Dollar Baby* despite the poor performance of boxing movies in the past—and especially of boxing movies that revolved around female fighters—no one at the studio had any idea it would become a box-office hit. If anyone other than Clint Eastwood had brought the movie to the studio, it likely never would have seen the light of day (or, rather, the darkness of a theater). Fittingly, when Warner threw Horn a good-bye party, George Clooney publicly thanked him for "supporting the things we want to do that studios never want to do." Smart A-list actors remember these sorts of gestures and become allies.

Finally, developing and releasing a number of smaller projects helps producers spread the fixed costs of their production and distribution infrastructures. For the major film studios that have expansive lots and dozens of offices around the world as part of their distribution apparatus, being able to allocate the costs of those resources across a larger number of projects—even if the smaller-scale projects barely break even—can be a huge benefit. For one, it helps them fund their blockbuster bets. "Very few entities in this world can afford to spend $200 million on a movie," noted Horn. "That is our competitive advantage."

Despite the advantages of having a broad and varied portfolio, major studios and other large-scale content producers would probably further tilt their investments toward the bigger projects if they could. But two key constraints make that difficult: raising the funds required to produce blockbusters is a constant challenge, and finding the ideas that lend themselves to bigger-scale production and marketing support is never easy. "We were keen to make more event films, and steadily increased the number over the years," Horn said about his time at Warner. "But there aren't many ideas with global appeal." What competing entertainment businesses do matters, too. As Horn pointed out: "There is a limit on good release dates in a given year."

And so, as a consequence of all these factors, many of today's largest entertainment businesses end up with product portfolios consisting of a few blockbuster investments that require most of their attention as well as a number of smaller bets. That's not to say that no other portfolio approach could possibly work. For example, animated movie house Pixar has an interesting approach: from the outset, it has focused on a very small number of films at any given time. Calling Pixar's strategy a "rifle-shot approach," Horn described its method this way: "They make one movie a year, and really handcraft each one. They are painstaking in their approach, highly self-critical, and work for years on one title before releasing it." That focus has paid off: Pixar has churned out one box-office smash hit after another, from *Toy Story* to *A Bug's Life*; *Monsters, Inc.*; *Finding Nemo*; *The Incredibles*; *Cars*; *Ratatouille*; *WALL-E*; *Up*; and

Brave. But Pixar is not a stand-alone studio: it operates as a unit at Disney and is now Horn's responsibility. Pixar thus can rely on the advantages that come with Disney's wider scale and power—a big plus, for instance, when it comes to distribution—while continuing to lavish attention on each of its films.

Another of Disney's units—Marvel Entertainment—is also a provider of a steady stream of huge hits. In fact, even more so than cats and dogs, comic-book heroes seem to be the favorite targets of Hollywood studios in search of the next blockbuster hit. The people behind the huge splash that the first *Spider-Man* movie made at the box office in 2002—and much of the superhero craze that followed in its footsteps—know a thing or two about creating and monetizing hits. The evolution of their business reveals just how dominant blockbusters have become and underscores many of the lessons learned about effective blockbuster portfolio strategies.

In August 2009, Disney announced a $4 billion purchase of Marvel Entertainment, which owned and managed one of the oldest and most recognizable collections of characters in the entertainment industry. Its proprietary library of thousands of characters, collectively known as the Marvel Universe, includes superheroes such as Spider-Man, X-Men, The Hulk, Daredevil, The Punisher, The Fantastic Four, Captain America, and Thor, all of which were developed for an astonishingly rich trove of comic books dating back to the 1930s.

As Disney's purchase of the company came together, Isaac Perlmutter, Marvel's chief executive officer and at the time its biggest shareholder, and his now former colleagues Avi Arad (who served as chief creative officer) and Peter Cuneo (who preceded Perlmutter as chief executive officer) had every reason to reminisce about a rescue they had staged that none of Marvel's superheroes could have pulled off—that of the company itself. Perlmutter and Arad had made their fortunes as partners in a toy company. With business experience in sectors such as fiberglass, pharmaceuticals, power tools, and electric shavers, Cuneo was as unlikely an entertainment mogul as one can find. But he was an expert at managing turnarounds, and that was his brief at Marvel when he joined the company in July 1999. He succeeded beyond all expectations: exactly a decade after Perlmutter and Arad acquired Marvel out of bankruptcy and hired Cuneo, and nine years after it posted a loss of over $100 million and saw its stock price hover at around $1, the Disney offer valued Marvel at around $50 per share. It was a performance that made the feats of both Spider-Man, with his ability to scamper up the sides of tall buildings, and The Hulk, with his unparalleled power (and greenness), seem decidedly mundane.

During that ten-year period, the executives rebuilt Marvel's original comic-book publishing business into a profitable division, and revamped its toy and licensing operations. Marvel lent its characters to twenty movies, including Sony Pictures' *Spider-Man*, Universal's *The Hulk*, Twentieth Century Fox's *X-Men*, and Lionsgate's *The Punisher*. Many movies recouped their costs by the time they closed out their domestic runs and went on to post big numbers in markets across the globe. Fourteen movies made more than $100 million in US theaters alone, six made more than $200 million, and four made more than $300 million. Remarkably, Marvel's sequels often outperformed its originals. As a result, worldwide grosses collected over a decade hovered close to the $7 billion mark.

Marvel also made licensing deals for a wide range of other products, from video games to apparel and from party items to food. "We contribute our characters and our knowledge of the characters, we work hard to find the right partners, and we approve the products for quality, but we don't contribute any capital," one Marvel executive told me. "We just collect checks." Perlmutter added: "It's a gold mine. Cash just comes in every day."

Within a few years of Cuneo's arrival, early doubts about the company's business model started to disappear. So did fears that the company had milked the best gains from its most prominent characters and might not be capable of further developing lesser-known superheroes such as Ghost Rider, Iron Man, The Punisher, and The Fantastic Four to boost growth. "There is no end to our success—we have a great library of characters," Arad told me in 2004. "I do feel frustrated by all the revenue that we are just giving away," he admitted, pointing to Marvel's relatively modest share of the revenues for its motion pictures. For instance, despite *Spider-Man*'s impressive theatrical box-office gross of over $820 million worldwide and sales of about 7 million $20 DVDs on the day of its release in the United States, Marvel received only about $25 million from Sony Pictures. "We have been focused on activities that require minimal capital investment on our part," said Cuneo at the time. "There are bigger bets to be placed as we move more into the production and distribution of content—but there could be bigger rewards, too."

In 2005, Marvel made its first strides toward that goal by landing $525 million worth of financing courtesy of Merrill Lynch that allowed it to produce its own film slate, and by giving Paramount Pictures the right to distribute those movies. Under the terms of the partnership, Marvel could produce up to ten movies over an eight-year period, with budgets ranging from $45 million to $180 million per film. Marvel received a fee for producing each film and would be able to keep all merchandising revenues, while Paramount collected a distribution fee of 8 percent of the box-office revenues for each film. (The deal also applied to any sequels to these films.) "Marvel has become a marquee entertainment brand," Paramount's chairman and chief executive officer, Brad Grey, said when the agreement was made public. "It speaks to Marvel's strength in the marketplace and the great popularity of its brand and characters that Marvel can obtain such innovative financing for its film slate. We are thrilled to partner with them in this new venture."

Further evidence of Hollywood's interest in Marvel's hit characters and story lines arrived four years later when Disney purchased Marvel. Despite the high purchase price, the agreement required Disney to honor Marvel's ongoing deals with other studios: Sony's right to make movies based on Spider-Man—Marvel's most sought-after character—lasts into perpetuity, and the deal with Paramount locked in several other characters. Yet Disney was

undeterred. As Bob Iger, Disney's chief executive officer, put it: "This treasure trove of over 5,000 characters offers Disney the ability to do what we do best."

Marvel's reversal of fortunes over the course of a decade—one of the greatest turnaround stories in the entertainment industry and indeed the business world in general—is a direct result of major movie studios' search for the next blockbuster. Basing a new event film on a Marvel character is now one of the surest bets a Hollywood executive can make. Ironically, the only major studio not mining Marvel's riches is Warner Bros.; its parent company, Time Warner, owns rival comic-book publisher DC Comics, which is known for Batman, Superman, and a host of other characters. Together, Marvel and DC have the market for comic books cornered.

It is too easy to dismiss Marvel as a company that simply got lucky with its *Spider-Man* franchise and since then just banked on that initial success. But the truth is that every studio head knows that the first *Spider-Man*—the highest-grossing film of 2002, and at the time the tenth-highest-grossing movie ever worldwide—single-handedly turned Sony Pictures' otherwise bleak year into a stellar one. In those early years, Marvel relied just as heavily on its biggest blockbuster. By my calculations, in fact, *Spider-Man* accounted for at least half of Marvel's operating income—measured across toys, media licensing, and consumer-products licensing—in 2002 and 2004, and at least a third of the company's operating income in 2003 (when no Spider-Man movie was released).

"It's toys, apparel, school products, games, promotions, pajamas, skateboards, vitamins, lollypops—with Spider-Man, there's virtually no limit," one of Marvel's consumer-products licensing experts told me. Cuneo agreed: "There is nothing close to Spider-Man. He is our number one character, with the widest demographic appeal of any fantasy property. His appeal starts with two-year-old children who wear Spider-Man pajamas and goes up to consumers in their sixties—they all enjoy Spider-Man. I wish all our characters were that broad."

Early successes triggered a superhero craze. As other Marvel movies such as *Daredevil*, *X2* (also known as *X-Men II*), and *The Hulk* performed well at the box office in the years following *Spider-Man*, and especially as the *X-Men* and *Blade* sequels outperformed their originals—a sign of a franchise having staying power or, as industry insiders say, "legs"—Hollywood executives began to compete ever more intensely for new Marvel characters that could be brought to the big screen. Marvel executives let the blockbuster trap work in their favor by pushing for better deal terms in negotiations with studios and other licensing partners. The original deals for *Blade* and *X-Men* stipulated that Marvel would receive a share of studio profits after all expenses had been incorporated. But studios had creative ways of calculating those profits that left only a negligible amount for Marvel—"Hollywood Economics," as Cuneo put it. With a few early movie successes under its belt, however, Marvel was able to negotiate more favorable revenue participation deals that gave it a share, typically between 3 and 7 percent, of box-office grosses for its blockbuster movies. This was still only a fraction of what the partnering studios were able to keep, but a definite improvement.

Meanwhile, Marvel executives created a business model that was specifically designed to minimize product-development and advertising costs—the major financial burdens involved in marketing blockbusters. Minimize those costs for Marvel, that is, and shift expenses to the studios that were licensing Marvel's characters. Here is how it worked. Marvel operated as a mini-conglomerate with divisions focused on comic books, toys, media licensing, and consumer-products licensing. The company developed its characters and story lines in its comic-book division, which effectively served as its research-and-development center, or as its incubator for ideas. And a highly efficient incubator at that, since comic-book publishing is relatively cheap and flexible: a typical print run costs the company only $10,000 to $20,000.

Marvel relied on partnering movie studios to advertise its brands. The company's licensing contracts with studios stipulated that Marvel did not contribute to movie production and marketing expenses. "Usually we get anywhere between thirty million and eighty million dollars in advertising devoted to our movies," Arad told me in 2004. "As a result, the word spreads like wildfire—it leads to worldwide exposure for the Marvel brand and for the specific character." Cuneo explained the resulting positive effect on its brands: "If you have seen our movies, you might get into our comic books, you might get into our video games, you might buy a T-shirt with a Marvel character, or you might buy some of the other consumer products."

How did Marvel make money? Although the partnering studios would undoubtedly have preferred otherwise, Marvel retained full control over merchandising rights, which it used to drive sales in toys and consumer products, the company's main sources of revenues. Consumer-products licensing in particular was—and is—a highly lucrative activity. Costs are incredibly low: at the time Disney made its move, Marvel's consumer media group (which coordinates activities for all consumer products) consisted of just a few salespeople and assistants, supported by a dozen or so legal and product-approval specialists. Contracts specified a minimum guarantee, to be paid to the rights owner regardless of the sales of the licensee's product, and additional royalties if sales exceeded the guarantee. Not surprisingly, the more the character was associated with blockbuster content, the higher both the minimum guarantee and the royalty rate that Marvel could negotiate. No wonder Perlmutter called it "a gold mine."

Marvel's approach to the management of its portfolio of brands was equally clever. Hollywood studio executives—and producers in many other sectors of entertainment—know that strong brands are not created overnight. For every *Finding Nemo*, which introduced a character that immediately resonated with audiences everywhere, there are hundreds of properties such as *Shark Tale* and *Delgo* that disappoint. Marvel's good fortune was that it had an extensive library of tried and tested characters and story lines to exploit, and Perlmutter, Arad, and Cuneo recognized this value. "We don't want to be a regular studio and come up with new ideas for movies," said Arad at the time. "Then we'll be like everybody else in this hit-and-miss business. That's a shot in the dark—we might as well play blackjack. Somehow the characters have permeated into our culture—that's our marketing advantage."

Blockbusters drove growth for other, lesser-known characters, building Marvel's portfolio over time. Helped by the fictitious Marvel Universe, which provided a common historical and contextual background for the company's characters, the executives emphasized the linkages that existed between its hit characters so as to grow smaller brands. (Elektra, for instance, made an appearance in the *Daredevil* movie and later starred in a movie of her own.) Cuneo explained the nature of the content library this way: "You've got to think of the forty-seven hundred characters not as individuals but as families. We have forty years of Spider-Man stories. There might be fifty bad guys associated with Spider-Man and fifty friends. So the Spider-Man family consists of one hundred, maybe two hundred, properties. The Hulk accounts for another hundred, while X-Men has about four hundred characters."

The essential natures of Marvel's franchise characters, built up over decades of appearances in comic books, are remarkably similar. As one Marvel executive put it: "They have some kind of vulnerability attached to them. Spider-Man is just a kid with glasses. Although they have superpowers, our characters are presented as normal people, with problems that anybody else would have." Because its brands are linked and in many respects similar, Marvel was in an ideal position to capitalize on Hollywood's search for the "next big thing" after the *Spider-Man* movie became a hit. Rather than fight against a blockbuster trap that was gaining momentum, the major studios helped to further strengthen Marvel's overall brand by pursuing the film rights to many of the company's other characters. Some marketing executives even asked for a Marvel-themed trailer to play just prior to their own films.

Realizing that bigger risks go along with bigger rewards, Marvel executives used their newfound powers to put together the groundbreaking deal with Paramount and Merrill Lynch—a move that fit Marvel's desire to capture more of the upside of its movies, but one that pitted the company directly against some of its other studio partners. By 2005, just a few short years after the first two

Spider-Man movies had together grossed more than $1.5 billion in worldwide ticket sales, Marvel's characters had become so sought-after that it could negotiate innovative financing: the contracts with Merrill Lynch reportedly stated that an insurer would cover interest payments in case Marvel would not be able to—in return for the movie rights to the central character. Have characters serve as collateral? It is hard to think of a more fitting illustration of the power of the company's blockbuster brands.

Further proving the strength of Marvel's characters, the first films to come out of the company's deal with Paramount—*Iron Man, Iron Man 2, Thor,* and *Captain America*—performed well, together collecting over $2 billion in global box-office revenues, over three times their estimated production costs. Coming at a time when Disney was struggling to generate hits of its own, Disney's bid for Marvel reflected the major studio's eagerness—or, given the billions of dollars involved in the transaction, some might say desperation—to call some of those blockbusters its own. In October 2010, less than a year after closing the purchase, Disney gained further control of the Marvel portfolio by buying Paramount out of its worldwide marketing and distribution rights for *The Avengers* and *Iron Man 3,* in return for at least $115 million in distribution fees. Before long, no one at Disney had any regrets about the investments: in 2012, the first *Avengers* movie raked in a staggering $1.5 billion in tickets; in 2013, *Iron Man 3* also crossed the $1 billion mark. Whatever the further fortunes of Marvel's resilient superheroes, the evolution of the company and its new life as a subsidiary of Disney underlines Hollywood's reliance on the kind of colossal hits that only Marvel's superheroes and Hollywood's smartest executives can make happen.

winner-take-all markets where being "average" is not good enough and scale is critical, where smart firms make blockbuster bets and put all their weight behind making those bets catch on with consumers, and where top-ranked individual performers—true superstars—are critical to success and may capture most of the rewards that are up for grabs. All in all, it is time to rewrite Irving Berlin's 1954 blockbuster *There's No Business Like Show Business*—the business world at large, it turns out, can learn quite a bit from the entertainment industry.

NOTES

In this book, I draw on hundreds of in-depth interviews I have conducted with entertainment executives, talent, and other personalities over the course of nearly a decade. Many of these interviews were a part of the case studies I developed in my role as a professor at the Harvard Business School; some interviews were conducted exclusively for the book. As is standard procedure with Harvard Business School cases, the interviewees have had a chance to review their quotes. The detailed notes below refer to the individual case studies.

I also rely on my analyses of sales and other quantitative data on the entertainment industry. Some of my findings have been published in scholarly articles in academic journals. The notes below provide information on both the data sources and the corresponding journal articles, and often provide additional details on the analyses.

Prologue: Show Business—a Business of Blockbusters

1 as Horn put it, "really pursued it as a strategy": Unless otherwise indicated, I obtained the quotes in this book from personal interviews.

3 "He's earned the respect of the industry for driving tremendous: Dawn C. Chmielewski, "Alan Horn Could Revive Walt Disney Studios' Magic," *Los Angeles Times*, June 1, 2012.

3 One rival executive labeled Zucker "a case study in the most destructive: Maureen Dowd, "The Biggest Loser," *New York Times*, January 12, 2010.

7 to crow about "an electricity in the building" at the company's headquarters: James B. Stewart, "NBC Finds a Winner in 'The Voice,'" *New York Times*, March 2, 2012.

Chapter One: Betting on Blockbusters

15 In June 2012, less than two weeks after the news of: This section is partly based on: Gary Pisano and Alison Berkley Wagonfeld, "Warner Bros. Entertainment," Harvard Business School Case 610-036. I identify each quote used from this case separately, but I think a wider acknowledgment of their work is appropriate. My own

interviews with Alan Horn, which are the source for the large majority of his quotes in the book, were conducted before he commenced his new role at Disney Pictures.

15 Disney Pictures had posted disappointing box-office results: Ryan Nakashima, "Disney Says 'John Carter' to Lose $200 million," *Associated Press*, March 19, 2012.

16 Described as "a consensus builder," Horn went to great lengths: Patrick Goldstein, "Alan Horn: Can Disney's New Boss Reinvent the Studio?," *Los Angeles Times, 24 Frames* blog, June 1, 2012.

16 The results proved the wisdom of his strategy: Warner Bros. press releases, boxofficemojo.com.

17 "Making monster projects into profit centers is no slam-dunk: Merissa Marr, "Warner's Event Movie Bet," *Wall Street Journal*, June 1, 2004.

17 Detractors of event-film strategies also loved to point to the western: Steven Bach, *Final Cut: Dreams and Disaster in the Making of Heaven's Gate* (New York: William Morrow & Co., 1985); "Review of 'Heaven's Gate,'" *Chicago Sun-Times*, January 1, 1981.

17 "In a good year, a major studio is happy to bat .500: Gary Pisano and Alison Berkley Wagonfeld, "Warner Bros. Entertainment," Harvard Business School Case 610-036.

18 "It is such a gut-level decision that it is impossible to define": The last sentence of this quote comes from ibid.

19 The studio released twenty-two films that year, spending about $1.5 billion: I estimated production budgets mentioned in this section using a variety of sources, including interviewees and other industry experts, boxofficemojo.com, the-numbers.com, imdb.com, annual reports, and trade magazines. Assessing production budgets is unavoidably an inexact science, though, so the numbers cited should be regarded as approximations. I obtained (proprietary) data on advertising spending from Kantar Media; I did not receive such data directly from Warner Bros. or any other studio.

20 "We have made a conscious decision at Warner Bros.: Gary Pisano and Alison Berkley Wagonfeld, "Warner Bros. Entertainment," Harvard Business School Case 610-036.

20 Although the top three biggest bets only accounted for a third: I obtained domestic box-office data from Rentrak, and international box-office estimates from boxofficemojo.com.

20 At the other extreme, the four least expensive movies released in 2010: Several of these movies were only distributed by Warner Bros. and not produced by Warner Bros. And although a twenty-third film, *Pure Country 2*, was a part of its slate that year, too, I have excluded it here because it saw virtually no theatrical release and was largely distributed in DVD format. Including the film would make the distribution of revenues and profits across films even more skewed.

21 The figure plots each of the 119 films that Warner: To construct the sample, using data provided by Rentrak, I first compiled a listing of all Warner Bros. movies that were theatrically released in the five-year window from January 1, 2007, through December 31, 2011, and then excluded rereleases and IMAX movies. I used various sources to compile the necessary data: domestic box-office revenues from Rentrak; foreign box-office revenues from boxofficemojo.com; and production-budget estimates from interviewees and other industry experts, boxofficemojo.com, the numbers.com, imdb.com, annual reports, and trade magazines.

22 *The Blind Side, The Hangover,* and *Gran Torino*: *The Blind Side* was distributed by Warner Bros. but produced by Alcon Entertainment.

23 The figure shows how much the 119 movies, when grouped: To illustrate the basic relationship between costs and revenues, I define "surplus" as the difference between worldwide box-office revenues and production expenditures. The metric is not meant to be taken literally as the profits that flow to the studio; note, for instance, that the metric does not account for the studio's advertising expenditures and the revenue share that the studio pays the theater.

24 "The advertising expenditures for a movie that cost $150 million to make: The same is true for distribution costs, which in the film industry come in the form of prints (or copies of the film): a more expensive film may be distributed more widely, meaning more prints are needed, but, again, distributing a more expensive film will be more cost efficient. When films are fully digitally distributed, making extra copies will be very inexpensive. This further increases the relative advantage of bigger releases.

25 The figure shows, for Warner's 2010 movie slate: I obtained data on advertising expenditures from Kantar Media. The data cover advertising expenditures across a range of media, including newspapers, magazines, network and cable television, radio, and outdoor.

28 "We intend to relax risk aversion policies: "Paramount Sees Its Future in the Stars," *New York Times*, March 31, 2004.

28 The latter was one of the biggest box-office disasters of all time: As estimated by boxofficemojo.com.

28 One of the most daring bids in the world of book publishing: I have earlier discussed some of these arguments in an article on blockbuster bets in book publishing: Anita Elberse, "Blockbuster or Bust," *Wall Street Journal*, January 3, 2009.

29 His charming, unassuming personality easily made up for it: This section is based on: Anita Elberse, "Grand Central Publishing," Harvard Business School Case 508-036.

29 Author advances in the tens of thousands: For more information on the structure of such contracts and the publishing industry more generally, see: Albert N. Greco, *The Book Publishing Industry*, 2nd ed. (Hillsdale, NJ: Lawrence Erlbaum, 2005); The Book Industry Study Group, "Book Industry Trends 2006"; *The Bowker Annual Library and Book Trade Almanac*, 51st ed., edited by Dave Bogart (Medford, NJ: Information Today, Inc., 2006); and Standard & Poor's "Industry Surveys: Publishing," March 8, 2007.

29 *Marley & Me* had garnered critical and commercial success: "Competitors Bark at Heels of 'Marley's' Success," *USA Today*, April 29, 2007.

30 William Morrow, a HarperCollins imprint, had paid: Ibid.

30 "It's stunning, the advances being paid: Motoko Rich, "Iowa Library's Cat Has a Rich Second Life as a Biography," *New York Times*, April 4, 2007.

30 According to Kosztolnyik's records, Peter Gethers' *The Cat Who Went to Paris*: These data are from Nielsen BookScan, the most comprehensive source of information on industry sales. BookScan does not cover all retailers, though; Walmart is an example of a retailer that is excluded.

31 A publisher's front list is its catalog of new books: Standard & Poor's, "Industry Surveys: Publishing," March 8, 2007.

31 Grand Central chose to compete this way in a sector where: The Association of American Publishers (AAP) collects monthly and annual data on book returns.

32 The sixth-highest-selling book (fiction or nonfiction) of 2006: I am indebted to Al Greco for his help in securing these Nielsen BookScan data.

34 and when a no-name filmmaker with a minuscule budget: *The Blair Witch Project* cost only $60,000 to produce and generated close to $250 million in worldwide box-office revenues. *Paranormal Activity* cost only $15,000 to produce and generated nearly $200 million at the box office worldwide. Even *Paranormal Activity 4*, made for $5 million, generated five times its production budget in its opening weekend alone.

35 Many movie lovers lament the offerings: These nine films were *Harry Potter and the Deathly Hallows: Part 2, Transformers: Dark of the Moon, The Twilight Saga: Breaking*

Dawn—Part 1, The Hangover Part II, Pirates of the Caribbean: On Stranger Tides, Fast Five, Mission: Impossible—Ghost Protocol, Cars 2, and *Sherlock Holmes: A Game of Shadows*.

36 "Sometimes this industry is like the mafia: Gary Pisano and Alison Berkley Wagonfeld, "Warner Bros. Entertainment," Harvard Business School Case 610-036.

37 When, in the mid-2000s, a brave producer: This paragraph is based on: Anita Elberse, "Xanadu on Broadway," Harvard Business School Case 508-062.

37 Described by influential film critics as "the epic failure: Roger Ebert, "Xanadu" Review, *Chicago Sun-Times*, September 1, 1980; Clark Collis, "Why People Love 'Xanadu,'" *Entertainment Weekly*, July 6, 2007.

38 "As soon as you say *Xanadu*," he remarked: Clark Collis, "Why People Love 'Xanadu,'" *Entertainment Weekly*, July 6, 2007.

38 When Ahrens approached Douglas Carter Beane: John Berman and Ted Gerstein, "Can Broadway Fix 'Xanadu'?," *ABC News*, July 9, 2007.

40 Literary agent Jonny Geller joked that his agency: *Sex Story: Fifty Shades of Grey*, Documentary, Channel 4, United Kingdom.

42 The above figure plots each of the sixty-one hardcover books: These data came directly from Grand Central Publishing; the sample covers all books on the publisher's fall 2006 front list.

42 because of the economies of scale involved in advertising campaigns: In video games, Activision Blizzard is an interesting example. Its three key franchise titles—*Call of Duty, World of Warcraft*, and *Skylanders*—accounted for approximately 73 percent of its net revenues and, according to the game publisher, "a significantly higher percentage" of its operating income in 2011. (Source: Activision's 2011 Annual Report.)

43 The figure shows how much the fall 2006 hardcover titles: Here, "costs" include the author's advance and royalty payments, printing and binding, freight and shipping, and marketing. "Net sales" are the net copies sold multiplied by the cover price, and taking into account any retailer discounts. "Gross profits" are the net revenues (which cover net sales and any subsidiary rights) minus paper, printing and binding, freight and shipping, marketing, and total author earnings.

44 Called *Dewey: There's a Cat in the Library*, it sold 106,000 copies: Again, I am indebted to Al Greco for his help in securing these Nielsen BookScan data.

44 At one point, there was even talk of a movie adaptation: Michael Fleming, "Meryl Streep to Star in 'Library Cat': Actress Purrs for New Line's 'Dewey,'" *Variety*, November 12, 2008.

45 Additionally, a larger number of products often leads to volume discounts: Savings on advertising are especially likely if studios can buy television advertising time on the so-called up-front advertising market (as opposed to the "scatter market"). A larger scale facilitates such media buys.

46 Large media producers may buy advertising time on television months in advance: Most television advertising is sold on the up-front market, which takes place in May each year, when the networks present their program lineups for the upcoming season.

48 In August 2009, Disney announced a $4 billion purchase: This section is based on: Anita Elberse, "Marvel Enterprises, Inc.," Harvard Business School Case 505-001.

48 As Disney's purchase of the company came together: "Marvel May Need Heroic Help," *Wall Street Journal*, June 29, 2004; "Shareholder Scoreboard: Leaders and Laggards in the Rankings," *Wall Street Journal*, March 8, 2004.

50 In 2005, Marvel made its first strides toward that goal: Marvel Enterprises, "Marvel Launches Independently Financed Film Slate with Closing of $525 Million Non-Recourse Credit Facility," press release, September 6, 2005.

51 "This treasure trove of over 5,000 characters offers Disney: David Goldman, "Disney to Buy Marvel for $4 Billion," *CNN Money*, August 31, 2009.

55 the first films to come out of the company's deal with Paramount: Marvel Enterprises, "Marvel Launches Independently Financed Film Slate with Closing of $525 Million Non-Recourse Credit Facility," press release, September 6, 2005.

55 Disney gained further control of the Marvel portfolio by buying Paramount: Pamela McClintock, "Move for Marvel Rights," *Variety*, October 18, 2010.

Chapter Two: Launching and Managing Blockbusters

56 Standing backstage at a sold-out concert in Boston's TD Garden: This section is based on: Anita Elberse and Michael Christensen, "Lady Gaga (A)," Harvard Business School Case 512-016; Anita Elberse and Michael Christensen, "Lady Gaga (B)," Harvard Business School Case 512-017.

57 Born as Stefani Joanne Angelina Germanotta in New York City: "Bio," www.ladygaga.com; "Lady Gaga: Biography," *Rolling Stone*. Both accessed May 31, 2011.

57 In 2003, she was one of twenty students given early admission: Vanessa Grigoriadis, "Growing Up Gaga," *New York Magazine*, March 28, 2010.

58 "May you always have soft cuticles while tweeting: Mawuse Ziegbe, "Lady Gaga Thanks Fans for Twitter Crown," MTV.com, August 22, 2011.

61 *My Big Fat Greek Wedding* is a classic example: For more information on this and other limited releases, see: Anita Elberse, John A. Quelch, and Anna Harrington, "The Passion of the Christ (A)," Harvard Business School Case 505-025; Anita Elberse, John A. Quelch, and Anna Harrington, "The Passion of the Christ (B)," Harvard Business School Case 505-026.

62 In the book business, the initial launch of E. L. James's mega-seller: Peter Osnos, "How 'Fifty Shades of Grey' Dominated Publishing," *Atlantic*, August 2012.

63 Carter and his team arranged for fifty popular music bloggers: Simon Owens, "The Secrets of Lady Gaga's Social Media Success," *The Next Web*, March 15, 2011.

63 *Just Dance* broke into major charts for dance airplay and club play: Jonathan Cohen, "Lady GaGa Dances to the Top of Hot 100," *Billboard*, January 8, 2009.

65 Spending ramps up dramatically in the six to eight weeks before release: In a 2007 academic article, I present data for a sample of 280 films in which 91 percent of spending takes place in the four weeks before release, 81 percent in the final three weeks, 62 percent in the final two weeks, and 34 percent in the final week. For more information, see: Anita Elberse and Bharat N. Anand, "The Effectiveness of Pre-Release Advertising for Motion Pictures: An Empirical Investigation Using a Simulated Market," *Information Economics and Policy* 19, nos. 3–4 (October 2007): 319–43.

65 In 2011, for example, the top hundred films, from *Harry Potter*: I conducted this analysis using rankings and box-office-revenues data pulled from boxofficemojo.com.

65 That, in turn, follows from the very nature of entertainment products: The economist Richard Caves has an in-depth examination of how properties of creative industries and creative goods drive business strategy: Richard E. Caves, *Creative Industries: Contracts Between Art and Commerce* (Cambridge, Mass.: Harvard University Press, 2000). Whereas Caves considers industrial-organization and contracting issues, my focus is on strategic marketing challenges.

66 For media products, initial success breeds further success: These ideas are explored in considerable detail in Robert H. Frank and Philip J. Cook, *The Winner-Take-All Society* (New York: Free Press, 1995).

66 When Disney's $250-million-budget *John Carter* generated a disappointing: Pamela McClintock, "Box Office Report: 'John Carter' Earns Weak $30.6 Mil Domestically, $101.2 Mil Globally," *Hollywood Reporter*, March 11, 2012.